

The Legality of Opportunistically Timing Public Company Disclosures in the Context of SEC Rule 10b5-1

By Allan Horwich*

Commentators have discovered that executives who engage in securities transactions purportedly under the shield of a Rule 10b5-1 Plan, so that their trades do not constitute unlawful insider trading, achieve abnormal returns. There is speculation that these returns may be achieved by influencing the timing of corporate disclosures, so that, for example, bad news is withheld at the corporate level until after a Plan sale occurs.

This article concludes that so long as this delay in disclosure does not violate an SEC mandated disclosure requirement, Rule 10b-5 is not violated, and the SEC could not expand Rule 10b-5 to reach disclosure timing of this type. The article also addresses the application of the common law to disclosure timing. The use of corporate information to time corporate disclosure for a personal benefit, to achieve a more favorable outcome in personal securities trading pursuant to a Plan, may be a breach of duty under the corporate common law of some states, including Delaware, applying established principles of the common law of insider trading. It is unlikely, if not impossible, however, that state regulatory authorities could or would pursue such conduct.

If remedial action is needed to discourage, and effectively preclude, disclosure timing, it should be in the nature of SEC mandated disclosures of information regarding Rule 10b5-1 Plans, something the SEC proposed more than ten years ago and then abandoned without explanation, and the exclusion of those who engage in disclosure timing from the benefits of Rule 10b5-1 by amending that rule itself.

Contents

I. Introduction—The Claimed Abuse of Rule 10b5-1	1114
II. An Executive’s Disclosure Timing for His Own Financial Benefit Does Not Violate the Federal Securities Laws.....	1120
A. General Principles of Disclosure Under the Federal Securities Laws	1120
B. The Salient Elements of Rule 10b-5.....	1122
C. The SEC’s Interpretation of Rule 10b5-1	1123

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D. An Analysis of Plan-Related Disclosure Timing Under the Securities Laws.....	1124
E. Stock Exchange Listing Agreements that Impose a Disclosure Obligation	1128
III. Under Existing Legislation the SEC Does Not Have the Authority to Amend Its Rules to Make Disclosure Timing for Personal or Corporate Benefit Wrongful; Some Options Are Available to Address Disclosure Timing	1130
A. Rule 10b5-1 Cannot Be Expanded to Make Plan-Related Disclosure Timing Unlawful	1130
B. The SEC’s Power to Expand the Reach of Rule 10b-5 Is Limited	1131
C. The SEC Has Some Limited Alternatives Under Current Law to Address Disclosure Timing in the Context of Rule 10b5-1 Plans	1133
1. Disclosure of Rule 10b5-1 Plans.....	1133
2. Amendment of Rule 10b5-1	1135
D. In the Absence of Amendments to the Securities Laws Plan-Related Disclosure Timing Will Remain Lawful.....	1136
IV. Disclosure Timing May in Limited Circumstances Breach a State Common Law Duty, Which in Any Event Is Not Enforced by Any Governmental Authority.....	1137
A. The Corporate Common Law Duty of Disclosure.....	1137
B. Option Backdating	1138
C. Option Spring-Loading and Bullet-Dodging.....	1141
D. The Corporate Opportunity Doctrine	1144
E. The Common Law of Insider Trading	1145
V. The Use of Corporate Information in Deciding to Cancel a Plan Is Not a Breach of Duty.....	1149
VI. State Enforcement Authorities Are Not Likely to Take Action to Obtain Sanctions for Mere Breaches of Fiduciary Duty	1149
VII. Conclusion.....	1150

I. INTRODUCTION—THE CLAIMED ABUSE OF RULE 10b5-1

Securities and Exchange Commission (“SEC” or “Commission”) Rule 10b-5,¹ adopted by the SEC pursuant to authority granted by section 10(b) of the Securi-

1. Rule 10b-5 states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

- (a) To employ any device, scheme, or artifice to defraud,
- (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
- (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (2016).

ties Exchange Act of 1934 (“Exchange Act”),² is a rule of wide impact. The SEC has the power to bring actions seeking a variety of civil remedies for a violation of the rule.³ The U.S. Department of Justice prosecutes criminal violations of the rule.⁴ Allegations of violations of Rule 10b-5 in civil and criminal enforcement actions include, among other claims, misrepresentations by companies and their executives that inflate the price of a company’s stock, where the executive profits from sales of the stock at those inflated prices. An example of this kind of claim is the charges leveled against Kenneth Lay, chairman and CEO of Enron Corp., who allegedly inflated the stock price of Enron in order to profit from personal stock sales.⁵ Similar claims have also been made in civil damages actions.⁶ *Pre-transaction* deception of this type is not addressed further in this article. Rather, this article addresses whether Rule 10b-5 reaches a different kind of influence over corporate disclosures that can also benefit an executive, or the corporation itself, when trading in the stock of the company. The focus here is on withholding the disclosure of bad news until after a pre-arranged trade is executed or accelerating the disclosure of good news before a pre-arranged trade is executed.

“Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud.”⁷ As a general principle, in the absence of an SEC rule requiring disclosure by a certain date, a public corporation has discretion when to disclose information regarding the business of the company.⁸ This raises the question

2. 15 U.S.C. § 78j(b) (2012).

3. Exchange Act § 21(d), 15 U.S.C. § 78u(d) (2012) (authorizing action in federal court for injunctive and other equitable remedies); *id.* § 21C, 15 U.S.C. § 78u-3 (2012) (authorizing administrative proceeding to impose cease-and-desist order and remedial measures). Civil monetary penalties may be imposed in either forum. *Id.* § 21(d)(3), 15 U.S.C. § 78u(d)(3) (authorizing judicial imposition of monetary penalties); *id.* § 21B(a)(2), 15 U.S.C. § 78u-2(a)(2) (2012) (authorizing SEC to impose monetary penalties in proceedings under section 21C). There are remedial provisions in the Securities Act of 1933, 15 U.S.C. §§ 77a et seq.; the focus here is on Exchange Act enforcement.

4. Exchange Act § 21(d)(1), 15 U.S.C. § 78u(d)(1) (“The Commission may transmit such evidence as may be available concerning such acts or practices as may constitute a violation of any provision of this title or the rules or regulations thereunder to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this title.”). For a description of the process of cooperation between the SEC and the Department of Justice (“DOJ”) in these respects, see Mary Jo White, Chair, U.S. Sec. & Exch. Comm’n, Speech—All-Encompassing Enforcement: The Robust Use of Civil and Criminal Actions to Police the Markets (Mar. 31, 2014), <http://www.sec.gov/News/Speech/Detail/Speech/1370541342996>.

5. See Press Release, Fed. Bureau of Investigation, Former Enron Chairman and Chief Executive Officer Kenneth L. Lay Charged with Conspiracy, Fraud, and False Statements (July 8, 2002), <https://www.fbi.gov/news/pressrel/press-releases/former-enron-chairman-and-chief-executive-officer-kenneth-l-lay-charged-with-conspiracy-fraud-false-statements> (reporting criminal charges); SEC Charges Kenneth L. Lay, Enron’s Former Chairman and Chief Executive Officer, with Fraud and Insider Trading, SEC Litig. Release No. 18776 (July 8, 2004) (reporting SEC civil enforcement charges).

6. See, e.g., *In re Enron Corp. Sec., Derivative & ERISA Litig.*, No. MDL-1446, Civ. A. No. H-01-3624, 2003 WL 21418157, at *15 (S.D. Tex. Apr. 24, 2003) (denying motion to dismiss Rule 10b-5 claim alleging that chairman and CEO sold company stock when he knew of nonpublic adverse information about the company, including transactions and practices carried out “for the purpose of manufacturing positive financial statements to deceive investors and creditors and enriching to an extraordinary degree the very people running the corporation”).

7. *Chiarella v. United States*, 445 U.S. 222, 235–36 (1980).

8. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 850 n.12 (2d Cir. 1968) (“the timing of disclosure is a matter for the business judgment of the corporate officers entrusted with the management of

whether Rule 10b-5, or any other provision of the federal securities laws, reaches the deliberate exercise of influence over the timing of disclosure by a public company (referred to throughout as “disclosure timing”) in order to achieve a benefit in open market stock trading by a corporate executive, by the corporation itself, or by a third party.

This activity may occur when the executive has a pre-established trading plan. In certain circumstances it is unlawful for a person to buy or sell a security “on the basis of” material nonpublic information, generally referred to as “insider trading.”⁹ In 2000, the SEC adopted Rule 10b5-1, which provides defenses in certain circumstances when an insider is aware of material nonpublic information at the time of her transaction and that awareness would otherwise result in liability for the trading under the classical or misappropriation theory of insider trading.¹⁰ Rule 10b5-1(b) provides that “a purchase or sale of a security of an issuer is ‘on the basis of’ material nonpublic information about that security or issuer if the person making the purchase or sale was aware of the material nonpublic information when the person made the purchase or sale.”¹¹ Rule 10b5-1(c) affords specific, purportedly exclusive, affirmative defenses to a charge of trading in violation of Rule 10b-5 “on the basis of” material nonpublic information where the person on whose behalf the trade was made was aware of the information at the time of the transaction. These defenses include establishing a securities trading plan at a time when the creator of the plan is *not* aware of material nonpublic information regarding the securities to be bought or sold. A Rule 10b5-1 plan (“Plan”) must specify parameters for purchases or sales on behalf of the creator of the Plan, to be carried out by a third person, such as a broker, without later influence by the person on whose behalf the trade is made.¹²

Consider the following scenarios:

A) A corporate executive has a valid Plan in effect to accomplish diversification of his portfolio. The Plan provides that the final sale of company stock under the Plan will occur on Wednesday morning at the then market price. During the preceding weekend the executive learns that the company has received notice from its largest customer that, in the ordinary course of the company’s business, the customer will

the corporation within the affirmative disclosure requirements promulgated by the exchanges and by the SEC”). While later cases have rejected some of the insider trading analysis in *Texas Gulf Sulphur* (see, e.g., *Chiarella*, 445 U.S. at 233 (implicitly rejecting the parity of information test endorsed by *Texas Gulf Sulphur*, 401 F.2d at 848)), this principle regarding the exercise of business judgment in making disclosure remains sound.

9. See, e.g., *Chiarella*, 445 U.S. at 228–29 (describing classical theory of insider trading in violation of Rule 10b-5); *United States v. O’Hagan*, 521 U.S. 642, 651–52 (1997) (describing misappropriation theory of insider trading in violation of Rule 10b-5). A comprehensive discussion of the law of insider trading is beyond the scope of this article. For a thorough discussion of that field of law, see DONALD C. LANGEVOORT, *INSIDER TRADING: REGULATION, ENFORCEMENT & PREVENTION* chs. 1–6 (2016).

10. 17 C.F.R. § 240.10b5-1 (2016).

11. Selective Disclosure and Insider Trading, Securities Act Release No. 33-7881, 65 Fed. Reg. 51716, 51727 (Aug. 24, 2000) (to be codified at 17 C.F.R. pts. 240, 243 & 249) [hereinafter *Adopting Release*].

12. See generally Allan Horwich, *The Origin, Application, Validity, and Potential Misuse of Rule 10b5-1*, 62 *BUS. LAW.* 913, 918–28 (2007).

not renew its requirements contract with the company. Public disclosure of this new, material¹³ information will surely cause the price of the stock to drop. The executive influences, even interferes with, the normal internal corporate disclosure decision-making process so that public disclosure of the customer's notice will not be made until after his stock is sold under the Plan as scheduled. As a result, the executive's sale is made at a higher price than would have occurred if the announcement of the customer's decision had been made on the company's normal, i.e., earlier, timetable for announcing bad news.

B) Another executive of a public company learns that his beloved brother is about to sell his stock in that company. The executive is aware that the company's largest customer has notified the company of its intent, in the ordinary course of the company's business, to purchase a substantial additional amount of product from the company in the coming year. The executive influences the normal, deliberative disclosure process so that the announcement of this material development is accelerated to occur before the brother's stock is sold.¹⁴ As a result, the brother's sale is made at a higher price than if the corporate announcement had been made on the usual timetable.

C) A corporation uses a Plan to implement a corporate stock repurchase program, recognizing that a corporation trading for its own account is constrained by the classical theory of insider trading under Rule 10b-5.¹⁵ When it adopted Rule 10b5-1, the SEC recognized that the rule's defenses could apply to a corporate stock repurchase program.¹⁶ The repurchase Plan includes provisions that assure compliance with the safe harbor from a manipulation charge pro-

13. A fact is material if "there is a substantial likelihood that a reasonable shareholder would consider it important" in making his investment decision. *Basic Inc. v. Levinson*, 485 U.S. 224, 231 (1988) (action under Rule 10b-5) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976) (action under the SEC proxy anti-deception rule, Rule 14a-9, 17 C.F.R. § 240.14a-9)). An omitted fact is material if there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Basic*, 485 U.S. at 231-32 (quoting *TSC Indus.*, 426 U.S. at 449). When determining the materiality of a contingent event, materiality depends on the magnitude of the event, should it occur, and the probability that it will occur assessed as of the time of the materially faulty disclosure. *Basic*, 485 U.S. at 238. Judgments *ex ante* about which facts are material under the securities laws are often complex and difficult. See Allan Horwich, *An Inquiry into the Perception of Materiality as an Element of Scierter Under SEC Rule 10b-5*, 67 *Bus. Law.* 1, 14-15 (2011) (discussing and collecting authorities regarding the difficulty of determining materiality); see also Dale A. Oesterle, *The Overused and Under-Defined Notion of "Material" in Securities Law*, 14 *U. Pa. J. Bus. L.* 167, 167 (2011) ("the case-law [of materiality under the federal securities laws] is quixotic at best, and fickle at worst").

14. The executive prudently does not inform his brother of this development, lest the outsider brother—selling without the shield of a Plan—be charged as a tippee of his insider brother, with the executive brother being an unlawful tipper acting in violation of Rule 10b-5. The extent to which any such tip would have been unlawful is beyond the scope of this article. The law of family and friend tipping is before the Supreme Court in *United States v. Salman*, 792 F.3d 1087 (9th Cir. 2015), *cert. granted in part*, 84 U.S.L.W. 3405 (U.S. Jan. 19, 2016) (No. 15-628).

15. See *Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1203-04 (1st Cir. 1996).

16. *Adopting Release*, *supra* note 11, at 51728. A recent study identified nearly 1,700 corporate repurchase programs pursuant to announced Plans between 2001 and 2013 and determined that in recent years approximately one quarter of corporate repurchase programs are conducted in part or in full using Plans. Alice Bonaimé & David Moore, *Preset Repurchase Plans and SEC Rule 10b5-1* 1, 9 (Jan. 1,

vided by Rule 10b-18.¹⁷ Prior to the last scheduled purchase under the Plan, the company defers release of some material good news about the company until after the transaction, a disclosure that would increase the stock price. As a result, the stock is repurchased at a lower price.

This article first addresses whether either of the actions by the executive or the action by the corporation violates the federal securities laws. That is, what is the lawful permissible scope of a public company executive's or corporation's exercise of discretion *under the federal securities laws* to time public disclosure with an intent to benefit the executive, the company, or others in an open market transaction in the company's securities? After concluding that the securities laws do not currently prohibit this behavior, and current rulemaking power could not be exercised to prohibit it, this article considers the application of common law doctrines.

The backdrop for this analysis is the suspicion that there is deliberate timing of corporate disclosures of the type described. Those who have examined director and executive trading in their firm's stock, pursuant to as well as outside of Plans, have concluded that many of those traders have reaped abnormal returns.¹⁸ Taking the results of these empirical analyses at face value presents the question of whether these results are achieved by unlawful activity in the context of implementing Plans.

There could be several explanations for the realization of abnormal gains when trading under a Plan, compared to the results of trading by outsiders.¹⁹ For example, where Rule 10b5-1 is relied upon the trader could have violated the fundamental condition of the rule that a valid Plan can be established only when the person is not aware of material nonpublic information.²⁰ An executive might create a Plan that will result in Plan sales before bad news *already known to the executive* is disclosed publicly, thus yielding a greater sale price than if the sale occurred after disclosure.²¹

2015) (unpublished manuscript available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2557005).

17. 17 C.F.R. § 240.10b-18 (2016).

18. The seminal article is Alan D. Jagolinzer, *SEC Rule 10b5-1 and Insiders' Strategic Trade*, 55 MGT. SCI. 224 (2009); see also Eliezer M. Fich, Robert Parrino & Anh L. Tran, *Timing Stock Trades for Personal Gain: Private Information and Sales of Shares by CEOs* 20, 23-24 (July 10, 2015) (unpublished manuscript available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2579047); Jonathan A. Milian, *Insider Sales Based on Short-Term Earnings Information*, 47 REV. QUANTITATIVE FIN. & ACCT. 109 (2016); Taylan Mavruk & H. Nejat Seyhun, *Do SEC's 10b5-1 Safe Harbor Rules Need to Be Rewritten?*, 2016 COLUM. BUS. L. REV. 133, 158-64.

19. Comparing insider sales pursuant to Rule 10b5-1 Plans to insider sales outside Plans may not provide a meaningful indication of whether those with Plans reap greater market rewards than do outsider traders, because insiders may be trading *outside* the Plans in a fundamental insider trading violation of Rule 10b-5. See *supra* text accompanying note 9; see also Fich et al., *supra* note 18, at 20 ("while there appears to be some opportunistic timing under 10b5-1 plans, opportunism seems more pronounced in the absence of such plans"). One commentator writing prior to the adoption of Rule 10b5-1 estimated that insider trading profits aggregated as much as \$5 billion a year. Jesse M. Fried, *Reducing the Profitability of Corporate Insider Trading Through Pretrading Disclosure*, 71 S. CAL. L. REV. 303, 323 (1998).

20. 17 C.F.R. § 240.10b5-1(c)(1)(i)(A) (2016) (imposing condition that the Plan be established "[b]efore becoming aware of the [material nonpublic] information").

21. If challenged, the executive might contend that at the time the Plan was established the evolving situation was not (yet) material. See *supra* note 13 (defining what facts are material, including in the context of an evolving situation).

While the SEC Staff announced many years ago that it will vigorously enforce compliance with Rule 10b5-1,²² I have found only two enforcement cases alleging noncompliance with Rule 10b5-1 in the fifteen years the rule has been on the books. Only one of the cases proceeded to judgment.²³ The second case was abandoned after the defendant died.²⁴ Compliance *vel non* with the rule is sometimes an issue in private damages litigation under Rule 10b-5, a topic beyond the scope of this article.²⁵

Another posited reason for the favorable trading results, which is the subject of speculation in some of the empirical studies and in other discussions of Rule 10b5-1,²⁶ is that the Plan creator knows when transactions will occur in compli-

22. In 2007 the director of the SEC division of enforcement announced that the SEC Staff was going to look “hard” at whether Plans “are being abused in various ways to facilitate trading based on inside information.” Linda Chatman Thomsen, Dir., SEC Div. of Enf’t, Remarks at the 2007 Corporate Counsel Institute 10 (Mar. 8, 2007), <http://www.sec.gov/news/speech/2007/spch030807lct2.htm>. For more recent remarks from the SEC, see Yin Wilczek, *No Conclusion on 10b5-1 Plans, but SEC Monitoring Situation, Official Says*, SEC. L. DAILY (BNA) (Apr. 19, 2013), <http://www.bna.com/securities-law-daily-p5944/> (reporting remarks of Thomas Kim, chief counsel of the SEC Division of Corporation Finance, that the SEC has not reached a conclusion as to whether there is abuse of Plans but the situation is “obviously something we’re going to watch” and if executives are using the program to conduct illegal stock trading based on material, nonpublic information, “we will do something about it”); David Hall, *The Morning Ledger: SEC Broadens Probe on Executive Trades*, WALL STREET J. (Feb. 5, 2013), <http://blogs.wsj.com/cfo/2013/02/05/the-morning-ledger-doj-vs-rating-firms/> (“The SEC is gathering data on a broad number of trades by corporate executives in shares of their own companies.”).

23. Press Release, U.S. Sec. & Exch. Comm’n, SEC Charges Former Countrywide Executives with Fraud; Former CEO Angelo Mozilo Additionally Charged with Insider Trading (June 4, 2009), <https://www.sec.gov/news/press/2009/2009-129.htm>; see Complaint at paras. 9, 111, 114–24, SEC v. Mozilo, No. CV 09-3994-JFW (MANx) (C.D. Cal. June 4, 2009), <https://www.sec.gov/litigation/complaints/2009/comp21068.pdf>; see also SEC v. Mozilo, No. CV 09-3994-JFW (MANx), 2010 WL 3656068, at *20 (C.D. Cal. Sept. 16, 2010) (denying motion to dismiss charge of unlawful trading in violation of Rule 10b-5 where a jury could find “Mozilo was aware of material, non-public information at the time he adopted or amended these trading plans”); Press Release, U.S. Sec. & Exch. Comm’n, Former Countrywide CEO Angelo Mozilo to Pay SEC’s Largest-Ever Financial Penalty Against a Public Company’s Senior Executive; Settlement Permanently Bars Mozilo from Future Officer or Director Service (Oct. 15, 2010), <https://www.sec.gov/news/press/2010/2010-197.htm> (announcing settlement of case, including claim against creator of 10b5-1 plan).

24. The SEC charged Kenneth Lay of Enron Corp. with, among other violations, amending plans when he was in possession of material nonpublic information concerning Enron’s deteriorating financial condition. SEC Charges Kenneth L. Lay, Enron’s Former Chairman and Chief Executive Officer, with Fraud and Insider Trading, SEC Litig. Release No. 18776 (July 8, 2004), <https://www.sec.gov/litigation/litreleases/lr18776.htm>. The SEC abandoned the case when Lay died. Plaintiff’s Notice of Voluntary Dismissal as to Defendant Kenneth L. Lay Only, SEC v. Lay, No. 4:04-cv-00284 (S.D. Tex. Dec. 23, 2009), ECF No. 43; Order of Dismissal (S.D. Tex. Jan. 7, 2010), ECF No. 44.

25. In private damages cases the plaintiff often alleges that the defendant’s scienter in violating Rule 10b-5 is demonstrated by, among other things, his unlawful insider trading; the defendant responds, sometimes in a motion to dismiss, that his trades were lawful because they were made in accordance with a Plan. See, e.g., *Simon v. Abiomed, Inc.*, 37 F. Supp. 3d 499, 524–25 (D. Mass. 2014) (dismissing Rule 10b-5 complaint for failure to plead scienter, taking into account that certain defendants’ sales were made pursuant to Plans), *aff’d sub nom. Fire & Police Pension Ass’n of Col. v. Abiomed, Inc.*, 778 F.3d 228 (1st Cir. 2015) (not addressing impact of Rule 10b5-1 Plans on the allegations); see also Stanley Veliotis, *Rule 10b5-1 Trading Plans and Insiders’ Incentives to Misrepresent*, 47 AM. BUS. L.J. 313, 332–41 (2010) (collecting and discussing judicial decisions in private damage actions that have addressed Rule 10b5-1).

26. See Fich et al., *supra* note 18, at 1, 3, 15; Jagolinzer, *supra* note 18, at 226, 227, 237; see also Veliotis, *supra* note 25, at 329 & n.77 (citing Horwich, *supra* note 12, at 950, where this author first

ance with the terms of his Plan and influences the timing of corporate disclosure to maximize profits of one or more trades under the Plan, such as delaying the release of bad news until after a Plan sale occurs.²⁷ An executive also might accelerate the disclosure of favorable news so that it is released before a sale under a Plan, an act that seems largely benign, at least in the sense that the market is informed sooner rather than later.

The hypotheticals present the question whether it is a violation of the securities laws to exercise influence over the timing of corporate disclosure for the purpose of improving the outcome of transactions made pursuant to the executive's Plan. This question is independent of the principle that if an executive delayed disclosure when there was a duty on his part to update prior corporate disclosure or to correct a prior incorrect disclosure, he may have violated Rule 10b-5 irrespective of his motivation to maximize his profits upon selling his own stock.²⁸

II. AN EXECUTIVE'S DISCLOSURE TIMING FOR HIS OWN FINANCIAL BENEFIT DOES NOT VIOLATE THE FEDERAL SECURITIES LAWS

A. GENERAL PRINCIPLES OF DISCLOSURE UNDER THE FEDERAL SECURITIES LAWS

A complete failure to speak, a pure omission, is a violation of Rule 10b-5 only if there is a duty to speak.²⁹ Thus, there is no obligation under the securities laws

addressed the subject of this article in very general terms); John P. Anderson, *Anticipating a Sea Change for Insider Trading Law: From Trading Plan Crisis to Rational Reform*, 2015 UTAH L. REV. 339, 362–63 (“Since insiders also control the timing of disclosures, [Rule 10b5-1] freed them to time the release of subsequently obtained material nonpublic information so as to maximize profits for their pre-arranged trades.”); Maureen McGreevy, *Insider Waiting: The New Loophole Under Rule 10b5-1* 15–16 (Feb. 2007) (unpublished manuscript available at http://works.bepress.com/cgi/viewcontent.cgi?article=1000&context=maureen_mcgreevy) (“The most logical explanation for these findings [of outsize returns realized in trades pursuant to Plans] is that some insiders manipulate the release of company information by withholding negative news until after the trades they have scheduled under their 10b5-1 plans are executed.” (footnote omitted)); Karl T. Muth, *With Avarice Aforethought: Insider Trading and 10b5-1 Plans*, 10 U.C. DAVIS BUS. L.J. 65, 69 (2009) (noting that among “the primary categories of problems that arise under 10b5-1 trading plans” is that “executives, rather than tampering with their plans, will simply adjust the release of news from the firm to suit the plan already in place”).

27. Plans are used much more often for stock sales than for purchases. Milian, *supra* note 18, at 112 n.11 (“pre-planned purchases are quite rare compared to pre-planned sales”). The type of disclosure timing addressed here could entail accelerating the disclosure of bad news before stock purchases, in order to take advantage of the lower stock price at the time of the purchase. It seems more likely that if there is undisclosed bad news about his company the insider creator of a purchase Plan would cancel the Plan altogether rather than hasten the disclosure and allow the purchase to proceed. For a discussion of the Rule 10b-5 implications of the cancellation of a Plan, see *infra* text accompanying notes 43–45. For a discussion of the common law implications of the cancellation of a Plan, see *infra* text accompanying notes 164–66.

28. See JOHN C. COFFEE, JR., HILLARY A. SALE & M. TODD HENDERSON, *SECURITIES REGULATION: CASES AND MATERIALS* 1063–64 (13th ed. 2015) (describing duty to update and duty to correct under Rule 10b-5); DONNA M. NAGY, RICHARD W. PAINTER & MARGARET V. SACHS, *SECURITIES LITIGATION AND ENFORCEMENT: CASES AND MATERIALS* 55–58 (3d ed. 2012) (same).

29. See, e.g., *Basic Inc. v. Levinson*, 485 U.S. 224, 239 n.17 (1988) (“Silence, absent a duty to disclose, is not misleading under Rule 10b-5.”); *In re Time Warner Inc. Sec. Litig.*, 9 F.3d 259, 267 (2d

to make a disclosure immediately or by a certain date unless (1) a specific SEC rule requires that disclosure be made at or before a time certain;³⁰ (2) a half-truth has been uttered, requiring disclosure of the additional information necessary in order to make the statement made not misleading;³¹ or (3) disclosure is (i) required by a duty to update a prior affirmative statement that is no longer accurate or (ii) required by a duty to correct a statement that was untrue when made.³² Neither a public company nor its executives has a general obligation to disclose an event simply because it is material, whether favorable or unfavorable³³:

Much of plaintiffs' argument reads as if firms have an absolute duty to disclose all information material to stock prices as soon as news comes into their possession. Yet that is not the way the securities laws work. We do not have a system of continuous disclosure. Instead firms are entitled to keep silent (about good news as well as bad news) unless positive law creates a duty to disclose.³⁴

Thus, when considering the issue of disclosure timing in this article, it is assumed here that there has not been a failure to make a disclosure of information in compliance with a deadline prescribed by an SEC mandatory disclosure rule, such as the general requirement that information required to be disclosed on Form 8-K be disclosed within four business days of the triggering event.³⁵ A failure to comply with the four-day or other applicable 8-K deadline subjects the violator to sanctions.³⁶ Unless Plan-related disclosure timing imposes a greater

Cir. 1993) ("a corporation is not required to disclose a fact merely because a reasonable investor would very much like to know that fact. Rather, an omission is actionable under the securities laws only when the corporation is subject to a duty to disclose the omitted facts.").

30. See, e.g., *infra* text accompanying notes 35–36 (discussing requirements of Form 8-K).

31. Under Rule 10b-5(b), it is unlawful "to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." A "half-truth" violates the rule. *First Va. Bankshares v. Benson*, 559 F.2d 1307, 1314 (5th Cir. 1977) ("a defendant may not deal in half-truths").

32. See *supra* text accompanying note 28.

33. The contractual obligation of a company with securities listed on a securities exchange to make prompt disclosure is discussed at *infra* text accompanying notes 65–73.

34. *Gallagher v. Abbott Labs., Inc.*, 269 F.3d 806, 808 (7th Cir. 2001).

35. *General Instruction B.1 to Form 8-K*, U.S. SEC. & EXCHANGE COMMISSION, <http://www.sec.gov/about/forms/form8-k.pdf> (last visited June 12, 2016). There are exceptions to the four-day rule. A filing under Item 7.01 mandated by Regulation FD, 17 C.F.R. pt. 243 (2016), must be made simultaneously with the event triggering the disclosure, or promptly, in some cases as soon as twenty-four hours, after discovery that a selective disclosure was made that requires a public disclosure. *Id.* § 243.101(a). Earnings press releases under Item 2.02(b) of Form 8-K must be furnished before the related earnings conference call. A Form 8-K under Item 4.02 to disclose an auditor's restatement letter must be filed within two days of the receipt of the letter.

A Form 8-K required by Item 5.02(c) to announce new officers may be deferred until another public announcement is made of the appointment. The financial statements of an acquired business, required by Item 9.01, must be filed no later than seventy-one calendar days after the date of the initial report of the acquisition on Form 8-K. An optional disclosure of a material event under Item 8.01 has no filing deadline.

36. See, e.g., Exchange Act § 15(c)(4), 15 U.S.C. § 78o(c)(4) (2012) (granting SEC authority to require a person to comply with the public company reporting provisions of the Exchange Act where the person was a cause of the failure to comply due to an act or omission the person knew or should have known would contribute to the failure); Press Release, U.S. Sec. & Exch. Comm'n,

duty, the corporation has the discretion to file any time within the applicable window.³⁷

B. THE SALIENT ELEMENTS OF RULE 10B-5

Some of those who comment on disclosure timing seem to accept without further analysis that disclosure timing to produce more favorable results under Plan transactions is lawful.³⁸ This article now tests that assumption.

The starting point of the analysis is the elements of an SEC enforcement action. There is enforcement liability where there has been material deception with scienter in connection with the purchase or sale of securities.³⁹ The element of scienter, which is an intent to deceive (uniformly held to include reckless conduct⁴⁰), is satisfied where there is a deliberate delay or accelera-

SEC Sanctions 10 Companies for Disclosure Failures Surrounding Financing Deals and Stock Dilution (Nov. 5, 2014), <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370543368026> (reporting settlement with ten companies for failure to comply with Form 8-K disclosure requirements; settlement imposed cease-and-desist orders and monetary penalties).

If an executive's disclosure timing causes the company to fail to comply with SEC disclosure requirements, there may have been a breakdown in the company's disclosure controls, required by Rule 13a-15(a), 17 C.F.R. § 240.13a-15(a) (2016), or Rule 15d-15(a), 17 C.F.R. §240.15d-15(a) (2016). "[T]he term disclosure controls and procedures means controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the [Exchange Act] is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms." Rules 13a-15(d), 15d-15(d), 17 C.F.R. §§ 240.13a-15(d), 240.15d-15(d) (2016). In each Form 10-Q and Form 10-K the principal executive officer and principal financial officer must certify that they have "[e]valuated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation." Rules 13a-14(a), 15d-14(a), 17 C.F.R. §§ 240.13a-14(a), 240.15d-14(a) (2016); Regulation S-K, Item 6.01(b)(31)(i), 17 C.F.R. § 229.601(b)(31)(i) (2016). As with any disclosure requirement under the Exchange Act, non-compliance or false certification could result in an SEC enforcement action. This article assumes that disclosure timing does not cause the company to fail to meet any SEC-mandated disclosure requirement. See *supra* text accompanying note 35.

37. "If a triggering event specified in one of the items of Form 8-K occurs within four business days before a registrant's filing of a periodic report, the registrant [may] disclose the event in its periodic report rather than a separate Form 8-K." *Exchange Act Form 8-K, Questions and Answers of General Applicability, Section 101.01*, U.S. SEC. & EXCHANGE COMMISSION, <https://www.sec.gov/divisions/corpfin/guidance/8-kinterp.htm> (last updated Apr. 2, 2008).

38. See, e.g., Anderson, *supra* note 26, at 387 (referring to "harmless acceleration or delay of disclosure that is otherwise permitted by disclosure rules"); McGreevy, *supra* note 26, at 17 ("As long as an insider in possession of material nonpublic information is toying with the timing of the release of company information, and is not adjusting the timing of his or her trades in company stock under a 10b5-1 plan, the insider is not violating Rule 10b5-1." (footnote omitted)).

39. SEC v. Wolfson, 539 F.3d 1249, 1256 (10th Cir. 2008) (footnote omitted). Additional elements must be established to prove a private claim for damages, principally reliance upon the misrepresentation or omission, economic loss, and loss causation. Stoneridge Inv. Partners, LLC v. Sci.-Atlanta, Inc., 552 U.S. 148, 157 (2008).

40. See NAGY ET AL., *supra* note 28, at 115–16 (stating that all courts of appeals that have decided the issue have held the scienter includes reckless conduct, albeit the definition of recklessness varies somewhat among the circuits). This question has been repeatedly reserved by the Supreme Court. See, e.g., Matrixx Initiatives, Inc. v. Siracusano, 131 S. Ct. 1309, 1323 (2011).

tion of disclosure—if the act was deceptive within the scope of the rule.⁴¹ There is no doubt that disclosure timing would be “in connection with” a completed Plan transaction.⁴² Thus, the focus of an analysis of whether Rule 10b-5 has been violated in the Plan/disclosure timing scenarios discussed here is on whether disclosure timing is unlawfully “deceptive.”

C. THE SEC’S INTERPRETATION OF RULE 10b5-1

The SEC Staff agrees that it is neither a violation of Rule 10b-5 nor non-compliance with Rule 10b5-1 for someone who has established a Plan to terminate the Plan for the purpose of aborting a sale that would have taken place pursuant to the Plan at a disadvantageous price. The SEC Staff stated:

After the written trading plan . . . has been in effect for several months, the person terminates the selling plan by calling the broker and canceling the limit order.

(a) Does the act of terminating a plan while aware of material nonpublic information result in liability under Section 10(b) and Rule 10b-5?

No. Section 10(b) and Rule 10b-5 apply “in connection with the purchase or sale of any security.” Thus, a purchase or sale of a security must be present for liability to attach. See *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975).⁴³

The creator can cancel the Plan and then make a non-Plan sale after the new information is disclosed, taking advantage of the price increase after the information is publicly disclosed, and there will be no violation of Rule 10b-5 for having traded while aware of material nonpublic information.⁴⁴

Cancelation is not without risk, however.

41. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197–215 (1975) (holding that defendant must act with scienter—an intent to deceive—in order to violate Rule 10b-5).

42. *SEC v. Zandford*, 535 U.S. 813, 822 (2002) (“It is enough that the scheme to defraud and the sale of securities coincide.”).

43. *Division of Corporation Finance: Manual of Publicly Available Telephone Interpretations, Fourth Supplement, Rule 10b5-1, Item 15(a)*, U.S. SEC. & EXCHANGE COMMISSION (Oct. 2000), <http://www.sec.gov/interps/telephone/phonesupplement4.htm>.

The holding in *Blue Chip Stamps*, cited by the Staff, addressed only the element of the standing of a private party to sue in an action under Rule 10b-5. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 725 (1975). Many years later the Court acknowledged that the ruling in that case was policy-driven and not an interpretation for all purposes of the concept of “in connection with a purchase or sale of any security” as that phrase is used in Rule 10b-5. See *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 84 (2006) (“The *Blue Chip Stamps* Court purported to define the scope of a private right of action under Rule 10b-5—not to define the words ‘in connection with the purchase or sale.’”). After *Dabit*, however, the Staff did not retract its interpretation.

44. The Staff’s interpretation has not met with universal approval. See, e.g., M. Scott Henderson, *The Changing Demand for Insider Trading Regulation*, in *RESEARCH HANDBOOK ON INSIDER TRADING* 230, 248 (Stephen M. Bainbridge ed., 2013) (“[T]here was no reason why the interpretations that led to the loopholes in the Rule needed to be decided the way they were. Canceling a planned trade under the Rule based on material, non-public information could be ‘in connection with the purchase or sale of a security,’ as required by statute for the SEC to act, even if it might not be for planned trades not under the Rule.”). No authority was provided to support this analysis, however. Perhaps he was thinking of *Dabit*. Other commentators also view the SEC Staff interpretation as providing a large loophole. See, e.g., Mavruk & Seyhun, *supra* note 18, at 182–83.

Termination of a plan, or the cancellation of one or more plan transactions, could affect the availability of the Rule 10b5-1(c) defense for prior plan transactions if it calls into question whether the plan was 'entered into in good faith and not as part of a plan or scheme to evade' the insider trading rules within the meaning of Rule 10b5-1(c)(1)(ii). The absence of good faith or presence of a scheme to evade would eliminate the Rule 10b5-1(c) defense for prior transactions under the plan.⁴⁵

D. AN ANALYSIS OF PLAN-RELATED DISCLOSURE TIMING UNDER THE SECURITIES LAWS

With this background, we can now consider whether disclosure timing to improve the outcome of Plan sales violates Rule 10b-5. First, Rule 10b-5 cannot prohibit conduct more broadly than the statutory provision under which it was promulgated, section 10(b) of the Exchange Act, authorizes. A rule under that statute can reach only conduct that is "manipulative" or "deceptive," the words used in the statute.⁴⁶ "Manipulation," "virtually a term of art when used in connection with the securities markets,"⁴⁷ generally refers to "practices, such as wash sales, matched orders, or rigged prices, that are intended to mislead by artificially affecting market activity,"⁴⁸ and "connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities."⁴⁹ Although what is under consideration in this article might be characterized colloquially as manipulation of the corporate disclosure process, the exercise of control over the timing of corporate disclosure is not what was meant by "manipulation" when Congress enacted section 10(b).

The remaining core question is whether deliberate disclosure timing to maximize profits under a Plan is deception, that is, an omission, half-truth, or misrepresentation, within the scope of Rule 10b-5.⁵⁰ A delay in disclosure designed to allow a planned sale to take place *before* the release of bad news that will cause the stock price to decline is wrongful if there was an *independent duty* for the insider to have made earlier disclosure. There is no such duty, as recognized in *Texas Gulf Sulphur*, in which the court stated that in the absence of actual insider trading there is discretion to make disclosure unless an express SEC rule requires

45. *Division of Corporation Finance: Manual of Publicly Available Telephone Interpretations, Fourth Supplement, Rule 10b5-1, Item 15(b)*, U.S. SEC. & EXCHANGE COMMISSION (Oct. 2000), <http://www.sec.gov/interps/telephone/phonesupplement4.htm>.

46. *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 472-73 (1977) ("the language of the statute must control the interpretation of the Rule" and the "language of § 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception").

47. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1975).

48. *Santa Fe Indus.*, 430 U.S. at 476.

49. *Hochfelder*, 425 U.S. at 199; see also *Hundahl v. United Benefit Life Ins. Co.*, 465 F. Supp. 1349, 1360 (N.D. Tex. 1979) (defining "manipulation" as "practices in the marketplace which have the effect of either creating the false impression that certain market activity is occurring when in fact such activity is unrelated to actual supply and demand or tampering with the price itself"), followed by *Regents of the Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372, 390-92 (5th Cir. 2007).

50. *Santa Fe Indus.*, 430 U.S. at 476 & n.15. This initial discussion focuses on clause (b) of Rule 10b-5. For a discussion of clauses (a) and (c) of the rule, see *infra* text accompanying notes 54-61.

disclosure.⁵¹ It is instructive that corporate option granting practices that may be questionable from a fiduciary duty perspective also do not violate Rule 10b-5, although the company may be required, as part of the SEC's mandatory disclosure regime, to disclose the practices.⁵²

There is one very important caveat to a preliminary conclusion that disclosure timing is not deception in violation of Rule 10b-5(b). Rule 10b5-1(c)(1)(ii) provides that the affirmative defenses afforded by a Plan are available only if the Plan was "entered into in good faith and not as part of a plan or scheme to evade the prohibitions of this section."⁵³ If *at the time the Plan was established* the creator of the Plan intended to influence corporate news releases to maximize profits or minimize losses under the Plan, someone who *did* later engage in disclosure timing to his advantage may face a challenge by the SEC to the *bona fides* of the creation of the Plan at its inception.

The conclusion that disclosure timing is not a half-truth or misrepresentation does not, however, end the inquiry under Rule 10b-5. These concepts arise principally under clause (b) of the rule. Clauses (a) and (c), respectively, more broadly prohibit "any device, scheme, or artifice to defraud" and any "act, practice, or course of business which operates or would operate as a fraud or deception."⁵⁴ Under these clauses "[c]onduct itself can be deceptive."⁵⁵ In order to violate either of these clauses, however, just as with clause (b), there must be some kind of deception.⁵⁶ Some courts have recognized the concept of "scheme liability" under

51. See *supra* text accompanying note 8 (addressing the customary scope of an executive's discretion with regard to the timing of public disclosure).

52. See Executive Compensation and Related Person Disclosure, Exchange Act Release No. 54302A, 71 Fed. Reg. 53158, 53163 (Sept. 8, 2006) (to be codified at 17 C.F.R. pts. 228, 229, 232, 239, 240, 245, 249 & 274) (discussing the requirement to disclose the timing of stock option grants when it is material to investors in the context of compensation disclosures); *infra* text accompanying notes 122–32 (discussing option backdating, spring-loading, and bullet-dodging under the common law).

One recent paper contains an analysis of Rule 10b-5 that urges a broad application of the rule to certain stock option granting practices. S. Burcu Avci, Cindy A. Schipani & H. Nejat Seyhun, *Ending Executive Manipulations of Incentive Compensation* 22–34 (Ross Sch. of Bus. Working Paper No. 1305, 2016), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2740637. The analysis in that paper does not address the reach of Rule 10b-5 to disclosure timing in the context of Plans. In arguing for the application of Rule 10b-5 to some practices in connection with option grants the paper advocates an application of Rule 10b-5 that the authors implicitly acknowledge would be an extension of the law, as they observe that the behavior they address "violates at least the spirit of § 10(b) . . . and SEC Rule 10b-5, if not the statute and the rule." Where, as the authors acknowledge, the SEC has not been aggressive in pushing for the application of Rule 10b-5, *id.* at 25–27, it seems unlikely that the courts will rely on the "purposes of § 10(b)" or "the economic purpose of insider trading prohibitions," *id.* at 30, 32, to give the rule an expansive interpretation. A comprehensive critique of the arguments in this paper is beyond the scope of this article.

53. 17 C.F.R. § 240.10b5-1(c)(1)(ii) (2016).

54. *Id.* § 240.10b-5(a), (c). These are the clauses on which the federal law of insider trading under Rule 10b-5 is based, not Rule 10b-5(b). *Chiarella v. United States*, 445 U.S. 222, 225–26 (1980); see also *Fried v. Stiefel Labs., Inc.*, 814 F.3d 1288, 1293 (11th Cir. 2016) ("Rule 10b-5(b) prohibits misrepresentations and omissions of material fact; it does not prohibit an insider's failure to disclose all material information before trading in its stock. Insider trading is actionable under Rule 10b-5(a) and (c).").

55. *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta, Inc.*, 552 U.S. 148, 157–58 (2008).

56. See *supra* text accompanying note 46.

clauses (a) and (c) where the conduct does not run afoul of clause (b). To establish liability under the scheme liability theory, a plaintiff must prove that “the defendant . . . engaged in conduct that had the principal purpose and effect of creating a false appearance of fact in furtherance of the scheme.”⁵⁷ “Broad as the concept of ‘deception’ may be, it irreducibly entails some act that gives the victim a false impression.”⁵⁸ SEC enforcement actions where a claim of scheme liability, or other liability predicated on clauses (a) or (c) of Rule 10b-5, was upheld do not suggest that interference with the normal course of corporate disclosure is deceptive conduct that violates the rule if there is no resulting affirmative deception of *the public*. These cases include creating sham transactions and funding a campaign of disseminating false information;⁵⁹ creating false credits, in order to deceive the company’s accountants, resulting in false *public* financial statements;⁶⁰ and instructing others to take action that falsified the corporation’s financial records and covered up the falsification, resulting in false *public* financial disclosures.⁶¹

In view of the principle that, in the absence of an SEC rule requiring disclosure, there is no duty to disclose material nonpublic information,⁶² corporate silence should not give rise to an assumption by investors that there is no undisclosed material information known to the company. Thus, silence, including delayed disclosure, does not create a “false appearance” of fact that there is no undisclosed material information known to the company. Investors cannot make an assumption either way, at least not one that supports a Rule 10b-5 claim. For these reasons, affecting the normal course of corporate disclosure for personal gain in a securities

57. *Simpson v. AOL Time Warner, Inc.*, 452 F.3d 1040, 1048 (9th Cir. 2006), *vacated & remanded on other grounds sub nom. Avis Budget Grp. Inc. v. Cal. State Teachers’ Ret. Sys.*, 552 U.S. 1162 (2008). Courts have “not allowed subsections (a) and (c) of Rule 10b-5 to be used as a ‘back door into liability for those who help others make a false statement or omission in violation of subsection (b) of Rule 10b-5.’” *SEC v. Kelly*, 817 F. Supp. 2d 340, 343 (S.D.N.Y. 2011) (quoting *In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472, 503 (S.D.N.Y. 2005)); see also *Pub. Pension Fund Grp. v. KV Pharm. Co.*, 679 F.3d 972, 987 (8th Cir. 2012) (“We join the Second and Ninth Circuits in recognizing a scheme liability claim must be based on conduct beyond misrepresentations or omissions actionable under Rule 10b-5(b).”).

The SEC, however, has taken a broader view that scheme liability exists even where the gravamen is a misrepresentation of the type addressed in Rule 10b-5(b). *In re Flannery, Securities Act Release No. 9689* (Dec. 15, 2014), 2014 WL 7145625, at *12 (3–2 decision with no dissenting opinion) (“we conclude that primary liability under Rule 10b-5(a) and (c) also encompasses the ‘making’ of a fraudulent misstatement to investors, as well as the drafting or devising of such a misstatement”), *vacated on other grounds*, 810 F.3d 1 (1st Cir. 2015).

58. *United States v. Finnerty*, 533 F.3d 143, 148 (2d Cir. 2008) (affirming judgment of acquittal entered by district court after jury found defendant guilty).

The “false impression” criterion remains prevalent. See *SEC v. Sullivan*, 68 F. Supp. 3d 1367, 1377 (D. Colo. 2014); *SEC v. Goldstone*, 952 F. Supp. 2d 1060, 1205, 1235 (D.N.M. 2013) (citing *Stone-ridge*, 128 S. Ct. at 770) (“To hold otherwise [than require a showing of creation of a false appearance by the defendant] would allow plaintiffs, such as the SEC, to overcome the Supreme Court’s sharp distinction between those who are primarily liable for engaging in deceptive conduct, and those who only aid and abet the primary violation of another.”).

59. *SEC v. Farmer*, No. 4:14-CV-2345, 2015 WL 5838867, at *15 (S.D. Tex. Oct. 7, 2015) (granting SEC’s motion for summary judgment), *appeal docketed*, No. 15-20620 (5th Cir. Oct. 28, 2015).

60. *SEC v. Familant*, 910 F. Supp. 2d 83, 86–87, 97 (D.D.C. 2013) (denying motion to dismiss).

61. *SEC v. Fraser*, No. CV-09-00443-PHX-GMS, 2010 WL 5776401, at *7–8 (D. Ariz. Jan. 28, 2010) (denying motion to dismiss in this respect).

62. See *supra* text accompanying notes 29–34.

transaction pursuant to a Plan does not violate Rule 10b-5, even if it is achieved through *internal* corporate deception, such as giving a corporate colleague, including a director, a false explanation for a delay in public disclosure. Internal deception of one's fellow officers or of directors, with no resulting deception of the public, does not constitute a violation of Rule 10b-5 where the transaction is in the public market, not with the corporation.⁶³

In summary, there has been no wrongful conduct, no deception, because there has been no failure to comply on a timely basis with any affirmative disclosure requirement imposed by the SEC's rules; there has been no affirmative public misstatement about the administration of the Plan, either at inception (which might impose a duty to update if the disclosed protocol is changed or breached) or later; and silence about disclosure timing does not breach any independent duty to disclose. Nor does any internal deception about the corporate disclosure process support a scheme liability claim where no false appearance is created in any public disclosure. No provision of or rule under the Exchange Act or the Securities Act of 1933 ("Securities Act") other than Rule 10b-5 is a plausible candidate for application to this situation.⁶⁴

63. Each public reporting company is required to "[d]isclose whether [it] has adopted a code of ethics that applies to the registrant's principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions." Regulation S-K, Item 406(a), 17 C.F.R. § 229.406(a) (2016). If the registrant has not adopted such a code of ethics, it must explain why it has not done so. *Id.* These disclosures are to be included in the annual Form 10-K at Item 10. Alternatively, this information can be incorporated by reference from the company's proxy statement. The company must file with the SEC any code that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, as an exhibit to its annual report, and post the text of the code on its website. Regulation S-K, Item 406(c)(1)–(2), 17 C.F.R. § 229.406(c)(1)–(2) (2016). Any amendment to or waiver, explicit or implicit, of the company's code must be disclosed on Form 8-K or on the company's website. See *Form 8-K, Item 5.05*, U.S. SEC. & EXCHANGE COMMISSION, <https://www.sec.gov/about/forms/form8-k.pdf> (last visited June 12, 2016). For this purpose, "[t]he term implicit waiver means the registrant's failure to take action within a reasonable period of time regarding a material departure from a provision of the code of ethics that has been made known to an executive officer." *Id.* (Instructions to Item 5.05).

These codes of ethics generally include a provision precluding use of corporate confidential information for personal use. See, e.g., NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL § 393A.10 (2016), http://nysemanual.nyse.com/lcm/Help/mapContent.asp?sec=lcm-sections&title=sx-ruling-nyse-policymanual_303A.10&id=chp_1_4_3_11 (providing that the "code of business conduct and ethics for directors, officers and employees" required of all listed companies must prohibit use of "corporate property, information, or position for personal gain"). Disclosure timing would violate such a code. Although it is unlikely that an explicit waiver would have been granted for this breach of the code requiring disclosure on Form 8-K, an implicit waiver as defined in Item 5.05 would occur, and must then be disclosed, if an executive officer learned of another covered officer's disclosure timing in connection with a Plan. The failure to make the required disclosure would expose the company to sanctions for non-compliance with an Exchange Act disclosure requirement. See *supra* note 36.

64. Securities Act § 17(a), 15 U.S.C. § 77q(a) (2012) (rendering unlawful essentially the same behavior with respect to offers and sales of securities as Rule 10b-5 does for purchases and sales of securities, except as to the element of culpability, which is not addressed in this article); see *SEC v. Spence & Green Chem. Co.*, 612 F.2d 896, 903 (5th Cir. 1980) ("[T]he proscriptions of section 17(a) are substantially the same as those of section 10(b) and rule 10b-5 . . ."). Indeed, the language of Rule 10b-5 was adapted from section 17(a). *NAGY ET AL.*, *supra* note 28, at 336.

E. STOCK EXCHANGE LISTING AGREEMENTS THAT IMPOSE A DISCLOSURE OBLIGATION

Before concluding the analysis of the scope of Rule 10b-5, and in particular concluding that there is no duty to speak that is enforceable under Rule 10b-5, it is important to take into account that companies that have listed their securities on registered exchanges undertake in the listing agreement with the exchange to abide by the rules of the exchange. A typical listing agreement provides: “The Applicant Issuer certifies that it understands and agrees to comply with all current and future rules, listing standards, procedures and policies of the Exchange as they may be amended from time to time.”⁶⁵ One of the rules referred to provides: “A listed company is expected to release quickly to the public any news or information which might reasonably be expected to materially affect the market for its securities. This is one of the most important and fundamental purposes of the listing agreement which the company enters into with the Exchange.”⁶⁶

A violation of an exchange prompt disclosure rule is enforceable by the exchange itself.⁶⁷ The NYSE Listed Company Manual expressly provides for delisting a security, the sanction available to the exchange, in the event of “[t]he failure of a company to make timely, adequate, and accurate disclosures of information to its shareholders and the investing public.”⁶⁸ While securities have been delisted for failure to satisfy the prompt public disclosure requirement,⁶⁹ one commentator has speculated that exchanges have disincentives to enforce their listing

65. New York Stock Exchange Listing Agreement for Domestic Company Equity Securities, Section 1, https://www.nyse.com/publicdocs/nyse/listing/Domestic_Co_Listing_Agreement.pdf (last visited June 12, 2016).

66. NEW YORK STOCK EXCHANGE LISTED COMPANY MANUAL § 202.05 (2016), <http://goo.gl/mlGoZF>; see also NASDAQ STOCK MARKET RULES § 5250(b)(1) (2016), <http://goo.gl/xZct7f> (“Except in unusual circumstances, a Nasdaq-listed Company shall make prompt disclosure to the public through any Regulation FD compliant method (or combination of methods) of disclosure of any material information that would reasonably be expected to affect the value of its securities or influence investors’ decisions.”).

67. See *In re N.Y. Stock Exch., Inc.*, Exchange Act Release No. 13346 (Mar. 9, 1977), 1977 WL 173602 (approving change to listing agreement and noting that the listing agreement “has traditionally been a principal means by which the NYSE enforces its listing standards”).

68. NYSE LISTED COMPANY MANUAL § 802.01D (2016), <http://goo.gl/S0sWqo> (granting the exchange “sole discretion” to delist the company); see also NASDAQ STOCK MARKET RULES § 5801 (2016), <http://goo.gl/nOZnBQ> (“Securities of a Company that do[] not meet the listing standards set forth in the Rule 5000 Series are subject to delisting from, or denial of initial listing on, the Nasdaq Stock Market.”); see *Fog Cutter Capital Grp. Inc. v. SEC*, 474 F.3d 822 (D.C. Cir. 2006) (denying petition for review of an SEC order dismissing the company’s application for review of NASD delisting of its public stock from Nasdaq). An exchange has absolute immunity from damages claims when it is exercising its authority under the Exchange Act to enforce its listing standards. See, e.g., *Weissmann v. Nat’l Ass’n of Sec. Dealers, Inc.*, 500 F.3d 1293, 1297–98 (11th Cir. 2007).

69. See, e.g., Press Release, Intercontinental Exch., NYSE to Suspend Trading Immediately in Lentuom International Inc. (LAS) and Commence Delisting Proceedings (Apr. 15, 2015), <http://ir.theice.com/press/press-releases/nyse-regulation/2015/suspensionlentuom> (announcing delisting on grounds including that issuer “failed to make timely, adequate, and accurate disclosures of information to its shareholders and the investing public, specifically regarding the January 2015 resignation of the Company’s independent public accounting firm”).

standards, with specific reference to the listing standard regarding timely public disclosures:

An exchange that sanctioned listed companies for fraud would expose those companies to class actions. A decision against a company would likely have res judicata effect in a subsequent class action, thus exposing the company to massive damages. . . . [T]he only sanction available to exchanges under current law is delisting, a draconian sanction that would punish shareholders without sanctioning wrongdoing managers. An effective enforcement regime requires a range of sanctions tailored to the offense. These sanctions would likely be unenforceable penalties if authorized only by the exchange listing agreement; the exchanges would need statutory authorization to fine-tune their sanctions.⁷⁰

That commentator's proposal, which has not gained traction and thus will not be discussed further here, was to shift investor recovery for securities fraud in the open market trading context from private class actions to exchange enforcement of listing standards.⁷¹

The contractual obligation imposed by the listing agreement to make prompt public disclosure of material events is not an undertaking enforceable by a private investor, complaining that he has been damaged by a corporation's failure to comply with that rule or that the exchange has failed to enforce it.⁷² Similarly, the listing standards do not create an obligation, the failure to comply with which is a breach of a duty to disclose that supports an SEC enforcement claim under Rule 10b-5 or any other provision of the Exchange Act. It is the province of the exchange to enforce its rules. While the exchange may be disciplined for the failure to do so,⁷³ the party whom the exchange should have disciplined does not, for that reason alone, become subject to liability under Rule 10b-5.

70. A.C. Pritchard, *Markets as Monitors: A Proposal to Replace Class Actions with Exchanges as Securities Fraud Enforcers*, 85 VA. L. REV. 925, 981–82 (1999) (footnotes omitted).

71. *Id.* at 983–86.

72. See, e.g., *State Teachers Ret. Bd. v. Fluor Corp.*, 654 F.2d 843, 852–53 (2d Cir. 1981) (rejecting implied federal cause of action by investor for company's failure to comply with the disclosure requirements of the listing exchange); *Jablon v. Dean Witter & Co.*, 614 F.2d 677, 681 (9th Cir. 1980) (rejecting investor's alleged implied cause of action under the securities laws for violation of rule of self-regulatory organization); see also COFFEE ET AL., *supra* note 28, at 686 (“SRO [such as securities exchange] regulations authorize only public enforcement and not private enforcement; [this] may arguably make it possible for SRO rules to establish more aspirational standards”); *id.* at 1043–44 (“[v]ritually every [appellate decision since *Jablon*] has agreed that there is no implied cause of action under the federal securities laws for a violation of an SRO rule” (footnote omitted)).

73. See, e.g., *In re N.Y. Stock Exch., Inc.*, Exchange Act Release No. 51524 (Apr. 12, 2005), 2005 WL 840452 (disciplining, in accordance with settlement, registered exchange for failure to enforce provisions of the Exchange Act and the exchange's own rules with respect to misconduct by exchange members).

III. UNDER EXISTING LEGISLATION THE SEC DOES NOT HAVE THE AUTHORITY TO AMEND ITS RULES TO MAKE DISCLOSURE TIMING FOR PERSONAL OR CORPORATE BENEFIT WRONGFUL; SOME OPTIONS ARE AVAILABLE TO ADDRESS DISCLOSURE TIMING

There is a subtext of a consensus among the commentators⁷⁴ that the exercise of discretion in timing public disclosure in order to benefit when making sales under a Plan *should be* prohibited. Because that conduct is not currently prohibited by the federal securities laws, as shown in Part II of this article, the next question is whether the SEC could prohibit this conduct under its existing authority. This presents the question whether the SEC has sufficient authority to revise Rule 10b5-1 itself or expressly define disclosure timing to be an “artifice to defraud” or a “course of business which operates or would operate as a fraud or deceit upon any person,” as those terms are used in Rule 10b-5. There are several impediments to these approaches.

A. RULE 10b5-1 CANNOT BE EXPANDED TO MAKE PLAN-RELATED DISCLOSURE TIMING UNLAWFUL

First, there are questions whether Rule 10b5-1 itself is a valid exercise of rulemaking in one or more respects.⁷⁵ Expanding that rule to define “fraud” or “deceit” in an unconventional way is not likely to enhance the validity of a rule that might otherwise be on shaky ground.

74. See *supra* notes 18 & 26.

75. See Horwich, *supra* note 12, at 943–49 (questioning validity of Rule 10b5-1 under *Chevron USA, Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984)); see also Ryan D. Adams, Comment, “Where There Is a Will, There Is a Way”: The Securities and Exchange Commission’s Adoption of Rule 10b5-1, 47 *LOY. L. REV.* 1133, 1151 (2001) (arguing that proof of “awareness” does not meet the scienter requirement); Deborah J. Jeffrey, *Knowing Too Much: New Rule on Insider Trading (Wrongly) Punishes for Possession of Information*, *LEGAL TIMES*, Nov. 20, 2000, at 34 (arguing that both use of the information and scienter are elements of an insider trading violation, and Rule 10b5-1 purports to dispense with both); Kimberly D. Krawiec & Richard W. Painter, *New SEC Regulations Attempt to Clarify Approach to Insider Trading*, 32 *SEC. REG. & L. REP.* (BNA) 1593, 1594 (Nov. 20, 2000) (“the awareness standard . . . arguably eliminates the scienter element from insider trading cases”); Stuart Sinai, *A Challenge to the Validity of Rule 10b5-1*, 30 *SEC. REG. L.J.* 261, 264–67, 271, 282 (2002) (arguing that Rule 10b5-1 removes the scienter requirement for insider trading, constitutes impermissible legislative action by the SEC, and effectively imposes strict liability for trading while in possession of material nonpublic information); Carol B. Swanson, *Insider Trading Madness: Rule 10b5-1 and the Death of Scienter*, 52 *U. KAN. L. REV.* 147, 196–99, 204 (2003) (criticizing Rule 10b5-1 as “duplicious,” questioning whether a trader who is aware of information but does not use it acts with scienter, and suggesting that Rule 10b5-1 “eliminates fraud from the liability standard” under Rule 10b-5); Kevin E. Warner, *Rethinking Trades “on the Basis of” Inside Information: Some Interpretations of SEC Rule 10b5-1*, 83 *B.U. L. REV.* 281, 305–15 (2003) (suggesting that Rule 10b5-1 may eliminate the requirement of scienter for an insider trading violation and offering interpretations of Rule 10b5-1 that do not abrogate the scienter requirement).

B. THE SEC'S POWER TO EXPAND THE REACH OF RULE 10B-5 IS LIMITED

More generally, the SEC's authority to adopt or to amend a rule pursuant to section 10(b) is constrained by the limits imposed by section 10(b).⁷⁶ In considering what section 10(b) permits the SEC to do is, it is important to keep in mind the distinction drawn in *O'Hagan* between the SEC's power under section 10(b), which authorizes the SEC only to proscribe acts that are *in fact* manipulative or deceptive devices or contrivances, and its broader power under section 14(e)⁷⁷ to prescribe means *reasonably designed to prevent* acts and practices that are fraudulent, deceptive, or manipulative.⁷⁸ This underscores the narrowness of the rule-making authority granted by section 10(b).

When the Supreme Court recently denied a petition for certiorari that raised the issue of the validity of Rule 10b5-1, Justice Scalia, joined by Justice Thomas, expressed concern about regulatory agencies specifying the elements of crimes through expansive rulemaking.⁷⁹

[L]egislatures, not executive officers, define crimes. . . . With deference to agency interpretations of statutory provisions to which criminal prohibitions are attached, federal administrators can in effect create (and uncreate) new crimes at will, so long as they do not roam beyond ambiguities that the laws contain. Undoubtedly Congress may make it a crime to violate a regulation [citation omitted] but it is quite a different matter for Congress to give agencies—let alone for us to presume that Congress gave agencies—power to resolve ambiguities in criminal legislation [citation omitted].

Whether or not Justice Scalia's concerns about the expansion of a prohibition with criminal law implications will carry the day, at the very least the Court has held that in adopting rules pursuant to section 10(b) the SEC is constrained to a concept of "deceptive" as it was understood by Congress when it adopted section 10(b) in 1934.⁸⁰

76. See *supra* text accompanying note 46; see also *United States v. O'Hagan*, 521 U.S. 642, 651 (1997) ("Liability under Rule 10b-5, our precedent indicates, does not extend beyond conduct encompassed by § 10(b)'s prohibition" of deceptive conduct.); *id.* at 655 ("[Section] 10(b) is not an all-purpose breach of fiduciary duty ban; rather it trains on conduct involving manipulation or deception.").

77. 15 U.S.C. § 78n(e) (2012) (providing in part, "[t]he Commission shall . . . by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative" in connection with tender offers).

78. *O'Hagan*, 521 U.S. at 671–73 ("We hold, accordingly, that under § 14(e), the Commission may prohibit acts not themselves fraudulent under the common law or § 10(b), if the prohibition is 'reasonably designed to prevent . . . acts and practices [that] are fraudulent.'").

79. *Whitman v. United States*, 135 S. Ct. 352, 353 (2014) (statement of Scalia, J., joined by Thomas, J., respecting the denial of certiorari). Of course, with the death of Justice Scalia his voice on this issue has been stilled.

80. See, e.g., *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 198 & n.20 (1975) (relying on 1934 dictionary definitions of terms used in section 10(b) in order to ascertain its scope), *cited in* *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 471 (1977) (stating that the starting point for the construction of section 10(b) is the language of the statute itself).

Use of a dictionary extant when the law was passed is a common approach when interpreting the federal securities laws. See, e.g., *Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension*

The SEC has sought to exercise broad authority in defining terms that are used by the courts in applying Rule 10b-5. In Rule 10b5-1 the SEC defined the term “based on” that had been *used by the courts* in defining unlawful insider trading.⁸¹ That phrase does not appear in any underlying SEC rule. Similarly, Rule 10b5-2 purports to define a term similar to one used by the courts in the application of the misappropriation theory of insider trading.⁸² In that rule the SEC defined the term “trust or confidence” to be applied *when the courts* refer to a breach of a duty of “trust and confidence” in determining whether material nonpublic information has been misappropriated in violation of Rule 10b-5.⁸³ It is far from free of doubt that a regulatory agency is entitled to judicial deference when defining words or phrases used *by courts* when those words or phrases do not appear in the relevant statute or rule.

At least two courts, however, have applied the SEC’s Rule 10b5-1 regulatory definition of “on the basis of” in an insider trading enforcement case not involving Rule 10b5-1 itself. In a criminal prosecution the court deferred to the SEC’s development of the “knowing possession” standard reflected in Rule 10b5-1.⁸⁴ More recently, a court held that in the absence of a definitive judicial construction of the phrase “on the basis of” the court would look to the SEC’s interpretation of the elements of the claim, even though the court did not then rigorously adhere to Rule 10b5-1 in all respects.⁸⁵

Fund, 135 S. Ct. 1318, 1325 (2015) (interpreting Securities Act of 1933); *Janus Capital Grp., Inc. v. First Derivative Traders*, 131 S. Ct. 2296, 2302 (2011) (interpreting Rule 10b-5, citing dictionaries from the 1930s); *Gustafson v. Alloyd Co.*, 513 U.S. 561, 575 (1995) (interpreting Securities Act); *Aaron v. SEC*, 446 U.S. 680, 696 n.13 (1980) (interpreting section 17(a) of the Securities Act).

81. See, e.g., *O’Hagan*, 521 U.S. at 658. The SEC’s position here is consistent with its longstanding view that trading while in possession of material nonpublic information is wrongful and that “use” of the information is not a necessary element when the other elements of the violation are established. See, e.g., *SEC v. Adler*, 137 F.3d 1325, 1332 (11th Cir. 1998) (“The SEC argues that the district court incorrectly adopted a causal connection standard for insider trading violations that allows a trader to avoid liability if the trader proves that he did not purchase or sell securities because of the material nonpublic information that the trader knowingly possessed.”).

82. 17 C.F.R. § 240.10b5-2(b) (2016) (defining the phrase “duty of trust or confidence”).

83. See, e.g., *O’Hagan*, 521 U.S. at 658 (referring to duty of “trust and confidence”); *Chiarella v. United States*, 445 U.S. 222, 233 (1980) (same).

84. *United States v. Royer*, 549 F.3d 886, 899 (2d Cir. 2008) (citing *United States v. Teicher*, 987 F.2d 112, 119–21 (2d Cir. 1993) (noting that Rule 10b5-1 was in accord with Second Circuit precedent on the meaning of Rule 10b-5)).

85. *SEC v. Moshayedi*, No. 12-01179, 2013 U.S. Dist. LEXIS 143624, at *42–44 (C.D. Cal. Sept. 23, 2013) (holding that where the pre-Rule 10b5-1 judicial construction did not find the statute to be unambiguous, the court would defer to the SEC’s subsequent rule, Rule 10b5-1, defining the phrase “on the basis of”).

At trial the court instructed the jury that knowledge of material nonpublic information at the time of the challenged transaction creates a “strong presumption that [the defendant] traded ‘on the basis of’ such information,” which can be rebutted if the defendant shows by a preponderance of the evidence “that he did not use” the information when he traded. On its face, this departs from Rule 10b5-1 in allowing exoneration of the defendant even if he did not establish one of the rule’s *exclusive* affirmative defenses. Jury Instructions, Instruction No. 24, *SEC v. Moshayedi*, No. 12-01179 (C.D. Cal. June 6, 2014), ECF No. 472. The jury found for the defendant. Final Judgment, *SEC v. Moshayedi*, No. 12-01179 (C.D. Cal. June 11, 2014), ECF No. 473.

Most recently, in *Fried*, the court noted, with reference to Rule 10b-5, that “the mere possession of material nonpublic information is not sufficient to establish liability for insider trading; an insider must use that information, although a strong inference of use arises when an insider trades while

While deference is accorded an agency's interpretation of its own rules,⁸⁶ an agency cannot overturn any unfavorable court decision through rulemaking.⁸⁷ Suffice it to say that the principles that govern the extent of judicial deference to agency action is an unsettled question.⁸⁸

C. THE SEC HAS SOME LIMITED ALTERNATIVES UNDER CURRENT LAW TO ADDRESS DISCLOSURE TIMING IN THE CONTEXT OF RULE 10b5-1 PLANS

Even if, as shown in the earlier sections of this article, the duplicitous timing of the release of news is not already within the scope of the Rule 10b-5 prohibitions and if the deception-based rules under the Exchange Act cannot be expanded to make this conduct unlawful, other regulatory changes might nevertheless be made to discourage or even deter timing the release of news in order to maximize profits under a Plan.

1. Disclosure of Rule 10b5-1 Plans

The SEC had proposed to require disclosure of Plans.⁸⁹ The proposed rule would have required that the issuer of the securities in question disclose “[e]ach director’s and executive officer’s adoption, modification or termination of

in possession of material nonpublic information.” *Fried v. Stiefel Labs., Inc.*, 814 F.3d 1288, 1295 (11th Cir. 2016) (citing *Adler*, 137 F.3d at 1338). Notably, one of the purposes of Rule 10b5-1 was to get around the ruling in *Adler*. See *Adopting Release*, *supra* note 11, at 51727 & n.97.

86. In *Bowles v. Seminole Rock & Sand Co.*, the Court held that in interpreting an administrative regulation

a court must necessarily look to the administrative construction of the regulation if the meaning of the words used is in doubt. The intention of Congress or the principles of the Constitution in some situations may be relevant in the first instance in choosing between various constructions. But the ultimate criterion is the administrative interpretation, which becomes of controlling weight unless it is plainly erroneous or inconsistent with the regulation.

325 U.S. 410, 414 (1945). This principle has been applied to adhere to an SEC interpretation of the SEC’s regulations under the Exchange Act. See *SEC v. McNulty*, 137 F.3d 732, 741 (2d Cir. 1998) (following *Seminole* in applying SEC regulations under section 13 of the Exchange Act, 15 U.S.C. 78m (2012)).

87. *Bankers Trust N.Y. Corp. v. United States*, 225 F.3d 1368, 1376 (Fed. Cir. 2000) (“we may not give . . . any executive branch agency the power to overrule an established statutory construction of the court”).

88. Three justices of the Supreme Court recently wrote in favor of reconsidering the prevailing caselaw of deference to an agency’s interpretation of its own rules. *Perez v. Mortgage Bankers Ass’n*, 135 S. Ct. 1199, 1210, 1211, 1213 (2015) (Alito, Scalia & Thomas, JJ., each separately concurring in the judgment). This salvo, as well as the statement by Justice Scalia in *Whitman* (see *supra* text accompanying note 79), is not the only attack from the conservatives on the Court on judicial deference to agency action. See, e.g., *Decker v. Nw. Env’tl. Def. Ctr.*, 133 S. Ct. 1326, 1338 (2013) (Roberts, C.J., concurring) (“Questions of *Seminole Rock* and [*Auer v. Robbins*, 519 U.S. 452 (1997)] deference arise as a matter of course on a regular basis. The bar is now aware that there is some interest in considering those cases . . .”).

89. One recent study suggests that, at least when disclosure of Plans has been made voluntarily, the creators of the Plans benefit, including achieving better returns on their trading. M. Todd Henderson, Alan D. Jagolinzer & Karl A. Muller, III, *Hiding in Plain Sight: Can Disclosure Enhance Insiders’ Trade Returns?* (Univ. of Chi. Law & Econ. Olin Working Paper No. 411, 2012), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1137928.

a contract, instruction or written plan for the purchase or sale of company equity securities intended to satisfy the affirmative defense conditions of Exchange Act Rule 10b5-1(c).⁹⁰ The proposal was never adopted, nor was it formally withdrawn.

Commentators concerned about the abuse of Plans recommend adopting the earlier proposal.⁹¹ Disclosure of Plans would give investors the opportunity to compare the dates of trades made pursuant to disclosed Plans to the timing of corporate disclosures and identify suspicious timing. SEC Form 4 requires prompt public disclosure of certain insider purchases and sales of beneficially owned equity securities.⁹² Disclosure of Plans together with the Form 4 filings could, at the very least, subject the trading insider to public scrutiny, even shaming. One proposal goes so far as to require that public companies report whether they have “withheld material information from the public for any reason, including coordinating its release with trades scheduled under 10b5-1 plans.”⁹³ A revelation of such a practice would be comparable to the current SEC requirement that a company disclose if it engages in questionable practices in granting employee stock options.⁹⁴

There is some voluntary disclosure of Plans. Sometimes this is done in a press release.⁹⁵ Form 4 does not require any disclosure of the use of a Plan. Some persons do follow the recommendation that transactions reported on Form 4 that have been made pursuant to a Plan be identified as such.⁹⁶ When Plan disclosures are made, however, the terms of the Plan are seldom revealed.

90. Form 8-K Disclosure of Certain Management Transactions, Exchange Act Release No. 8090, 67 Fed. Reg. 19914, 19915 (proposed Apr. 23, 2002) (to be codified at 17 C.F.R. pts. 230, 239 & 249).

91. This suggestion has been made in, e.g., Mavruk & Seyhun, *supra* note 18, at 182–83; Letter from Council of Institutional Investors to Mary Jo White, Chair, U.S. Sec. & Exch. Comm’n 2 (May 9, 2013), http://www.cii.org/files/issues_and_advocacy/correspondence/2013/05_09_13_cii_letter_to_sec_rule_10b5-1_trading_plans.pdf (“Companies and company insiders should disclose Rule 10b5-1 program adoptions, amendments, terminations and transactions”); Letter from Council of Institutional Investors to Elisse B. Walter, Chair, U.S. Sec. & Exch. Comm’n 1 (Dec. 28, 2012), <https://www.sec.gov/rules/petitions/2013/petn4-658.pdf> (“10b5-1 program adoptions, amendments, terminations and transactions should be disclosed immediately”); McGreevy, *supra* note 26, at 19; Muth, *supra* note 26, at 82; Jane Trueper, Comment, *10b5-1 Plans: Further Obscuring the “Smoking Gun” and Proposals for Change*, 16 U. PA. J. BUS. L. 937, 969–70 (2014).

92. The disclosure requirement applies to directors, certain officers, and persons who beneficially own more than 10 percent of the equity securities of most public reporting companies. Exchange Act § 16(a)(1), 15 U.S.C. § 78p(a)(1) (2012). See generally Rules 16a-3(a), (g)(1), 17 C.F.R. § 240.16a-3(a), (g)(1) (2016) (describing the transactions to be reported on Form 4). Rule 16a-1(f) narrowly defines “officer” for this purpose. 17 C.F.R. § 240.16a-1(f) (2016). A brief delay in filing the Form 4 is available for certain transactions executed pursuant to a Plan. Rule 16a-3(g)(2)–(4), 17 C.F.R. § 140.16-3(g)(2)–(4) (2016).

93. McGreevy, *supra* note 26, at 20–21 (footnote omitted).

94. See *supra* text accompanying note 52.

95. See, e.g., Press Release, Mellanox Techs., Ltd., Mellanox Technologies Executive Officers Adopt 10b5-1 Stock Trading Plans (Oct. 28, 2015), <http://www.businesswire.com/news/home/20151028006520/en/Mellanox-Technologies-Executive-Officers-Adopt-10b5-1-Stock>.

96. See, e.g., MORRISON & FOERSTER, FREQUENTLY ASKED QUESTIONS ABOUT RULE 10b5-1 PLANS 8 (2015), <http://media.mofo.com/files/Uploads/Images/FAQ10b51.pdf> (“It is advisable to specifically note on the Form 4 or 5 that the trades were made pursuant to a Rule 10b5-1 plan to ensure that investors

Above a certain threshold anticipated sales made pursuant to SEC Rule 144 must be reported in advance on Form 144.⁹⁷ That form contains a reference to Rule 10b5-1, which requires disclosure only of the date the Plan was adopted, not the terms of the Plan.⁹⁸ The Plan may have been adopted long before any actual sale.

2. Amendment of Rule 10b5-1

Another means of reducing disclosure timing in the context of a Rule 10b5-1 Plan would be to revise Rule 10b5-1 so that the affirmative defenses provided by the rule are not available to someone who engages in disclosure timing in connection with a Plan transaction. This would not make disclosure timing itself deceptive; as shown above Rule 10b-5 does not reach that behavior.⁹⁹ Rather, amending the rule would deprive the creator of a Plan of the benefit of the shield that Rule 10b5-1 provides in those cases where that person influences the timing of disclosure with the intent of achieving a more favorable outcome of a trade made pursuant to a Plan than would have been the case in the absence of disclosure timing.¹⁰⁰ A proviso in a revised Rule 10b5-1 that accomplishes this

or analysts monitoring sales by insiders will know that the trades do not represent a current investment decision by the insider.”).

For an example of this type of voluntary reporting, see SEC Form 4 report of sale of stock in Facebook Inc. by Marc L. Andreessen (Nov. 12, 2015), <http://d11ge852tjjqow.cloudfront.net/CIK-0001326801/34552583-b423-403f-baae-74490e1efe50.pdf> (including statement, “[t]he sales reported were effected pursuant to a Rule 10b5-1 trading plan adopted by the reporting person”).

97. 17 C.F.R. § 230.144 (2016) (providing exemption from the registration requirement of section 5 of the Securities Act of 1933, 15 U.S.C. § 77e (2012), for certain stock sales by affiliates of the issuer, among others). Rule 144(h)(1) requires that sales by an affiliate of the issuer in reliance on the exemption from registration provided by Rule 144 where “the amount of securities to be sold in reliance upon this rule during any period of three months exceeds 5,000 shares or other units or has an aggregate sale price in excess of \$50,000” be reported on Form 144 and transmitted to the SEC “concurrently with either the placing with a broker of an order to execute a sale of securities in reliance upon this rule or the execution directly with a market maker of such a sale.” 17 C.F.R. § 230.144(h).

98. Form 144 includes the following attestation:

The person for whose account the securities to which this notice relates are to be sold hereby represents by signing this notice that he does not know any material adverse information in regard to the current and prospective operations of the Issuer of the securities to be sold which has not been publicly disclosed. If such person has adopted a written trading plan or given trading instructions to satisfy Rule 10b5-1 under the Exchange Act, by signing the form and indicating the date that the plan was adopted or the instruction given, that person makes such representation as of the plan adoption or instruction date.

Form 144, U.S. SEC. & EXCHANGE COMMISSION, <https://www.sec.gov/about/forms/form144.pdf> (last visited June 12, 2016).

99. See *supra* text accompanying notes 46–64.

100. The rule could contain a proviso at the end of Rule 10b5-1(c)(1) such as the following: Provided, however, that the affirmative defenses in paragraph (c)(1) of this Section shall not be available to a person who, (I) with knowledge of when a future purchase or sale of securities on his behalf will take place in accordance with a contract, instruction, or plan described in paragraph (c)(1)(ii)(A) of this Section, (II) intentionally caused the delay of public disclosure of material nonpublic information for the purpose of gaining a greater profit or avoiding a greater loss on a transaction executed on his behalf that was otherwise in accordance with paragraph (c)(1) of this Section.

may, however, be difficult for enforcement authorities to apply with success. Among other factors, a delay in public disclosure of only a few hours or even a few minutes might be all that the creator of the Plan needs to reap a greater profit on a sale pursuant to a Plan. Proving that the person deliberately interfered with the normal disclosure process to that limited extent may be challenging, just as the SEC has, it appears, been unable to identify abuse of Rule 10b5-1 in its present form.¹⁰¹ Nevertheless, both requiring disclosure of Plans and amending Rule 10b5-1 as suggested may dampen any disclosure timing.

D. IN THE ABSENCE OF AMENDMENTS TO THE SECURITIES LAWS PLAN-RELATED DISCLOSURE TIMING WILL REMAIN LAWFUL

There is substantial empirical evidence that trades executed in accordance with the terms of Plans produce abnormally favorable outcomes. Speculation that these Plans are simply not being established or implemented in compliance with the law, and thus the transactions are really unlawful insider trading schemes, is not borne out by any SEC enforcement sweep.

Among the other reasons posited for these trading results is that insiders engage in disclosure timing to produce more favorable trading outcomes. Disclosure timing to enhance the profitability of sales that do not otherwise violate the securities laws is not deception in violation of Rule 10b-5. It is questionable that under existing regulatory authority disclosure timing to enhance outcomes under Plan trading can be made unlawful by rule. One practical, albeit only indirectly prophylactic, solution to any problem of disclosure timing is to require some disclosure of trading pursuant to Plans, at least by affiliates¹⁰² of an Exchange Act reporting company¹⁰³ that as a control person may be in a position to affect the timing of corporate disclosure.

This required disclosure could be as streamlined as what the SEC had proposed in 2002.¹⁰⁴ Experience may suggest that more is needed to facilitate public scrutiny of whether creators of Plans are tinkering with the timing of corporate disclosure to improve the outcome of Plan transactions. If so, an appropriate balance between the benefits of disclosure and the preservation of some degree of financial privacy for the creator of the Plan to effect lawful transactions could be a corporate Form 8-K¹⁰⁵ required to be filed no later than four business days after the Plan is executed, identifying the person who created the Plan, whether

101. See *supra* text accompanying notes 22–24 (noting only two cases alleging noncompliance with the rule when creating a Plan).

102. Under the Exchange Act, “[a]n ‘affiliate’ of, or a person ‘affiliated’ with, a specified person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.” Exchange Act Rule 12b-2, 17 C.F.R. § 240.12b-2 (2016).

103. A reporting company is a company required to file Exchange Act reports pursuant to section 13, 15 U.S.C. § 78m (2012), or section 15(d), 15 U.S.C. § 78o(d) (2012), of the Exchange Act.

104. See *supra* text accompanying note 89–90.

105. This element would indirectly impose a requirement on a director or officer of the issuer to make the necessary timely disclosure to the issuer, and would effectively preclude Plans that allowed for Plan transactions as soon as four days after execution.

the Plan provides for the purchase or sale of securities, or both, identifying the class(es) of securities covered by the Plan, the earliest date on which a transaction may occur under the Plan, and any fixed Plan termination date.¹⁰⁶ The SEC could also amend Rule 10b5-1 to deprive disclosure-timers from the benefits of the rule, though there is little cause for optimism that this would deter those who create Plans from engaging in disclosure timing.

IV. DISCLOSURE TIMING MAY IN LIMITED CIRCUMSTANCES BREACH A STATE COMMON LAW DUTY, WHICH IN ANY EVENT IS NOT ENFORCED BY ANY GOVERNMENTAL AUTHORITY

Conduct in connection with a securities transaction that does not violate the federal securities laws may, nevertheless, be wrongful, such as in breach of a fiduciary duty to the corporation.¹⁰⁷ This article now turns to common law issues, some of which have intersected with the federal securities laws. The focus here will be on Delaware law.¹⁰⁸

There are a number of contexts that merit consideration in seeking insight into whether Plan-related disclosure timing breaches a common law duty. They are the common law duty of corporate disclosure, option backdating, option spring-loading, option bullet-dodging, corporate opportunity, and insider trading.

A. THE CORPORATE COMMON LAW DUTY OF DISCLOSURE

As under the federal securities laws,¹⁰⁹ there is no general obligation under Delaware corporate law to make disclosure of material facts. In the leading Delaware case, *Malone v. Brincat*,¹¹⁰ the Delaware Supreme Court held:

The directors of a Delaware corporation are required to disclose fully and fairly all material information within the board's control when it seeks shareholder action. When the directors disseminate information to stockholders when no stockholder

106. Other elements could be required, such as disclosure of the total number of shares or other securities subject to the Plan and requiring updating of any material changes to the information before the Plan expires, including early termination of the Plan. The precise elements would be the subject of a proposed rule and public comment before any final rule could be adopted. See *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCHANGE COMMISSION, <http://www.sec.gov/about/whatwedo.shtml> (last visited June 12, 2016) (including explanation of SEC formal rulemaking process).

Consideration of whether any particular Plan-related disclosure requirement would exceed the SEC's rulemaking authority under section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a) (2012), is beyond the scope of this article, which does not offer a specific proposed rule.

107. As noted earlier, a breach of fiduciary duty without deception in connection with the purchase or sale of a security does not violate Rule 10b-5. See *supra* note 46.

108. Because the preponderance of public companies are organized under Delaware law, *Why Businesses Choose Delaware*, DEL.GOV, http://corplaw.delaware.gov/eng/why_delaware.shtml (last visited June 12, 2016) ("more than 60 percent of the Fortune 500 companies are incorporated in Delaware"), when general common law concepts are discussed in this article the focus will be Delaware law.

109. See *supra* text accompanying notes 29–32.

110. 722 A.2d 5 (Del. 1998).

action is sought, the fiduciary duties of care, loyalty and good faith apply. Dissemination of false information could violate one or more of those duties.¹¹¹

A claim for a breach of duty in connection with a disclosure that does *not* seek stockholder action requires an allegation of damage to the company.¹¹² There is thus no corporate law duty to disclose facts unless one is seeking shareholder action or otherwise making an affirmative disclosure that is deceptive without further disclosure.¹¹³ None of these factors is present when an executive engages in Plan-related disclosure timing where there has not been any public disclosure of the procedures to be followed in implementing the Plan.

B. OPTION BACKDATING

Employee stock options backdating, a practice that implicates both the Exchange Act and corporate law, garnered significant attention of stockholders and regulators beginning in 2005.¹¹⁴ In an attempt to boost the value of options to employees where the exercise price of the option was the market price of the stock on the date of the option grant, some companies backdated the date of the option grant to a day when the price of the company's stock was lower than the market price when the backdating occurred. Backdating for the purpose of setting an option exercise price lower than it should have been can result in un-

111. *Id.* at 12 (footnotes omitted). As one commentator summarized the law:

In Delaware, under the duty of candor, directors owe a fiduciary duty to disclose all material information to shareholders when: (1) seeking shareholder approval of transactions that cannot proceed without a shareholder vote; (2) seeking shareholder ratification of otherwise invalid or suspect transactions, such as self-dealing transactions or executive compensation and stock option plans; and (3) voluntarily communicating to shareholders, or the market generally, about the business of the corporation, even if no shareholder action is sought.

Shannon Germana, *What They Don't Know Can Hurt Them: Corporate Officers' Duty of Candor to Directors*, 34 DEL. J. CORP. L. 221, 233 (2009).

112. *Brincat*, 722 A.2d at 14; see generally R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, BALOTTI AND FINKELSTEIN'S DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 17.2 (2016) (discussing fiduciary duty of disclosure under Delaware law).

113. See generally J. ROBERT BROWN, THE REGULATION OF CORPORATE DISCLOSURE § 11.04[3] (3d ed. 2016) (discussing the duty to disclose when seeking shareholder action, in securities transactions, and a duty to correct prior statements in order to make them not misleading). It is a common law breach of duty in Delaware and some other jurisdictions for an insider, and thus presumably the corporation, to trade in its securities without disclosing nonpublic material information. See *infra* text accompanying notes 138–46; see also Germana, *supra* note 111, at 233 (“majority shareholders owe a duty to disclose all material information to minority shareholders when making a tender offer for their shares”).

114. For general discussions of the history of the backdating scandal and some of the legal issues raised by backdating, see Avci et al., *supra* note 52, at 1–10, 22–49; Lara E. Muller, Comment, *Stock Option Backdating: Is the Government's Response Enough to Eliminate the Problem or Is It Still a Work in Progress?*, 51 SANTA CLARA L. REV. 331 (2011). Jagolinzer noted the similarity of his analysis of trading pursuant to Plans to the analysis of suspect option grant activity. Jagolinzer, *supra* note 18, at 228. Several commentators studied whether disclosure timing affected the pricing of stock options, other than in the context of backdating of options. They concluded that the discretionary timing of disclosures to prospectively affect the stock price at the time of an executive compensation option grant did not violate the federal securities laws or state law. Charles M. Yablon & Jennifer Hill, *Timing Corporate Disclosures to Maximize Performance-Based Remuneration: A Case of Misaligned Incentives?*, 35 WAKE FOREST L. REV. 83, 91–103 (2000).

derstated compensation expense and overstated corporate earnings in public disclosures.¹¹⁵

In a leading decision regarding a common law backdating claim the court summarized the claims as follows:

The shareholder-approved 1983 Stock Option Plan and 1999 Stock Incentive Plan bound the board of directors to set the exercise price according to the terms of the plans. . . . Plaintiff alleges that from 1998 to 2002, the board actively allowed [the company] to backdate at least nine option grants issued to Gifford [chairman and CEO], in violation of shareholder-approved plans, and to purposefully mislead shareholders regarding its actions. As a result of the active violations of the plan and the active deceit, plaintiff contends that [the company] received lower payments upon exercise of the options than would have been received had they not been backdated. Further, [the company] suffers adverse effects from tax and accounting rules. The options priced below the stock's fair market value on the date of the grant allegedly bring the recipient an instant paper gain. At the time, such compensation had to be treated as a cost to the company, thereby reducing reported earnings and resulting in overstated profits. This likely necessitates revision of the company's financial statements and tax reporting. Moreover, Gifford, the recipient of the backdated options, is allegedly unjustly enriched due to receipt of compensation in clear violation of the shareholder-approved plans.¹¹⁶

In denying the motion to dismiss in significant part,¹¹⁷ the court held:

115. Muller, *supra* note 114, at 331–32. One notable enforcement action involved Brocade Communications Systems, Inc. The government alleged that Brocade engaged in routine backdating of stock option grants to give employees favorably priced options without recording the necessary compensation expenses. Press Release, U.S. Sec. & Exch. Comm'n, U.S. Attorney's Office and SEC Separately Charge Former Brocade CEO and Vice President in Stock Option Backdating Scheme (July 20, 2006), <https://www.sec.gov/news/press/2006/2006-121.htm>. The SEC's claims were ultimately settled. See, e.g., Court Enters Final Judgment Settling Action Against Defendant Gregory Reyes, SEC Litig. Release No. 22119 (Oct. 11, 2011), <https://www.sec.gov/litigation/litreleases/2011/lr22119.htm> (reporting that CEO Reyes agreed to an injunction from violating various provisions of the federal securities laws; to pay disgorgement, prejudgment interest and a civil penalty; and to be barred for ten years from acting as an officer or director of a public company); see also Brocade to Pay \$7 Million Penalty to Settle Charges for Fraudulent Stock Option Backdating, SEC Litig. Release No. 20137 (May 31, 2007) (reporting separate SEC settled enforcement action against the company for falsifying its reported income, with the company agreeing to an injunction from violating various provisions of the federal securities laws and to pay a \$7 million penalty). The CEO of Brocade was convicted of securities fraud. *United States v. Reyes*, 660 F.3d 454 (9th Cir. 2011).

The charges spawned civil damages litigation under Rule 10b-5 and state common law. *In re Brocade Commc'ns Sys., Inc. Derivative Litig.*, 615 F. Supp. 2d 1018 (N.D. Cal. 2009) (granting in part and denying in part motions to dismiss action brought on behalf of the company, taken over by a special litigation committee, against former officers and directors of Brocade alleging, among other claims, violation of Rule 10b-5, breach of fiduciary duties of care and loyalty, and unjust enrichment). The case was ultimately settled with substantial payments by or on behalf of various defendants. See, e.g., *In re Brocade Commc'ns Sys., Inc. Derivative Litig.*, No. 3:05-cv-02233 CRB (N.D. Cal. Dec. 21, 2009), ECF No. 467 (order approving settlement upon payment of \$12,500,000 by defendant Reyes).

116. Ryan v. Gifford, 918 A.2d 341, 347–48 (Del. Ch. 2007).

117. Claims of flawed grants before the stockholder plaintiff became a stockholder of Maxim were dismissed for lack of standing. *Id.* at 358–59.

Based on the allegations . . . the intentional violation of a shareholder approved stock option plan, coupled with fraudulent disclosures regarding the directors' purported compliance with that plan, constitute conduct that is disloyal to the corporation and is therefore an act in bad faith. . . . To make matters worse, the directors allegedly failed to disclose this conduct to their shareholders, instead making false representations regarding the option dates in many of their public disclosures.

I am unable to fathom a situation where the deliberate violation of a shareholder approved stock option plan and false disclosures, obviously intended to mislead shareholders into thinking that the directors complied honestly with the shareholder-approved option plan, is anything but an act of bad faith. It certainly cannot be said to amount to faithful and devoted conduct of a loyal fiduciary. Well-pleaded allegations of such conduct are sufficient, in my opinion, to rebut the business judgment rule and to survive a motion to dismiss.¹¹⁸

The court also observed:

A director who approves the backdating of options faces at the very least a substantial likelihood of liability, if only because it is difficult to conceive of a context in which a director may simultaneously lie to his shareholders (regarding his violations of a shareholder-approved plan, no less) and yet satisfy his duty of loyalty. Backdating options qualifies as one of those "rare cases [in which] a transaction may be so egregious on its face that board approval cannot meet the test of business judgment, and a substantial likelihood of director liability therefore exists."¹¹⁹

Plan disclosure timing does not involve conduct comparable to backdating. When there is Plan-related disclosure timing neither the board nor the executive is constrained by some stockholder approved plan, nor are any public disclosures made regarding compliance with a Rule 10b5-1 Plan. Rather, the executive has chosen from among otherwise lawful dates that comply with the federal securities laws to make, or at least influence the timing of, a corporate disclosure that provides a greater benefit to him than some other permissible date. The architect of disclosure timing in the Plan context, like the non-director executive who falsifies documents to backdate options, may in some situations deceive others *within the company* in order to implement his scheme, for example by falsely explaining why he is dragging his feet in signing off on disclosure, but not deceive an outsider.¹²⁰ Another distinction is that unlike the options backdating context the executive who engages in Plan disclosure timing has not harmed or imposed a cost on the corporation, or even exposed it to litigation for faulty financial disclosure. Executives' Rule 10b5-1 Plan transactions are gen-

118. *Id.* at 358–59. The case was eventually settled in exchange for cash payments to the company and for the cancellation, re-pricing, or surrender of options granted to the individual defendants. Ryan v. Gifford, No. 2213-CC, 2009 WL 18143 (Del. Ch. Jan. 2, 2009) (approving settlement and denying objection of a stockholder who was a plaintiff in a federal court derivative action).

119. *Ryan*, 918 A.2d at 355 (footnote omitted) (quoting *Aronson v. Lewis*, 473 A.2d 805, 815 (Del. 1984)).

120. *See supra* notes 57–64 and accompanying text (discussing the absence of implications under Rule 10b-5 for such an internal affirmative falsehood). Any breach of duty here seems best assessed under the rubric of the breach of loyalty implicated by insider trading. *See infra* text accompanying notes 136–63.

erally not ones with the company as the counterparty, and so the company is unaffected by the price at which securities are bought or sold under a Plan.¹²¹

C. OPTION SPRING-LOADING AND BULLET-DODGING

In “spring-loading” the corporate board grants options with exercise prices based on the then-current market price, acting with knowledge that the market price at the time of grant does not reflect favorable information about the company that has not yet been disclosed. The leading decision held:

Granting spring-loaded options, without explicit authorization from shareholders, clearly involves an indirect deception. A director’s duty of loyalty includes the duty to deal fairly and honestly with the shareholders for whom he is a fiduciary. It is inconsistent with such a duty for a board of directors to ask for shareholder approval of an incentive stock option plan and then later to distribute shares to managers in such a way as to undermine the very objectives approved by shareholders. This remains true even if the board complies with the strict letter of a shareholder-approved plan as it relates to strike prices or issue dates.

. . . The relevant issue is whether a director acts in bad faith by authorizing options with a market-value strike price, as he is required to do by a shareholder-approved incentive option plan, at a time when he knows those shares are actually worth more than the exercise price. A director who intentionally uses inside knowledge not available to shareholders in order to enrich employees while avoiding shareholder-imposed requirements cannot, in my opinion, be said to be acting loyally and in good faith as a fiduciary.

[In order to state a claim for a breach of duty in a spring-loading case] a plaintiff must allege that options were issued according to a shareholder-approved employee compensation plan. Second, a plaintiff must allege that the directors that approved spring-loaded (or bullet-dodging) options (a) possessed material non-public information soon to be released that would impact the company’s share price, and (b) issued those options with the intent to circumvent otherwise valid shareholder-approved restrictions upon the exercise price of the options. Such allegations would satisfy a plaintiff’s requirement to show adequately at the pleading stage that a director acted disloyally and in bad faith and is therefore unable to claim the protection of the business judgment rule.¹²²

Thus, an element of the misconduct in some cases of spring-loading is noncompliance with “a shareholder-approved employee compensation plan,” entailing

121. Plans are often used to effect the exercise of stock options. See, e.g., *Rule 10b5-1 Trading Plans*, BAIRD, <http://www.rwbaird.com/ci/executive-services/rule-10b5-1.aspx> (last visited Mar. 7, 2016) (stating that Plans may be used to exercise employee stock options). The option exercise price has already been set; thus, while any influence by the executive over the timing of disclosure may impact the market resale price of the stock acquired upon exercise, his action does not impact the price paid to the company for the stock when the option is exercised. This is independent of whether any duty was breached when the exercise price was set, e.g., by backdating.

122. *In re Tyson Foods, Inc. Consol. S’holder Litig.*, 919 A.2d 563, 592–93 (Del. Ch. 2007) (denying motion to dismiss in relevant part) (emphasis added) (footnotes omitted). The case was settled. *In re Tyson Foods, Inc. Consol. S’holder Litig.*, No. 1106-CC, 2008 WL 2914648 (Del. Ch. Apr. 11, 2008).

“avoiding shareholder-imposed requirements” that option grants provide for an exercise price equal to the “fair market value” of the stock on the day of the grant.¹²³

In a later opinion in the case, denying defendants’ motion for judgment on the pleadings, the court expanded on the scope of the duty of disclosure in a spring-loading context:

Loyalty. Good faith. Independence. Candor. . . . It is against these standards, and in this spirit, that the alleged actions of spring-loading or backdating should be judged.

. . . .

. . . Had the 2000 Tyson Stock Incentive Plan never been put to a shareholder vote, the nature of a spring-loading scheme would constitute material information that the Tyson board of directors was *obligated to disclose to investors when they revealed the grant*. By agreeing to the Plan, shareholders did not implicitly forfeit their right to the same degree of candor from their fiduciaries.

. . . Where a board of directors intentionally conceals the nature of its earlier actions, it is reasonable for a court to infer that the act concealed was itself one of disloyalty that could not have arisen from a good faith business judgment. The gravamen of [the spring-loading breach of duty claim] lies in the charge that defendants intentionally and deceptively channeled corporate profits to chosen executives Proxy statements that display an uncanny parsimony with the truth are not “analytically distinct” from a series of improbably fortuitous stock option grants, but rather raise an inference that directors engaged in later dissembling to hide earlier subterfuge. The Court may further infer that grants of spring-loaded stock options were both inherently unfair to shareholders and that *the long-term nature of the deceit* involved suggests a scheme inherently beyond the bounds of business judgment.

. . . [In light of additional information now before the court] I am not convinced that allegations of an implicit violation of a shareholder-approved stock incentive plan are absolutely necessary for the Court to infer that the decision to spring-load options lies beyond the bounds of business judgment. Instead, I find that where I may reasonably infer that a board of directors *later concealed the true nature of a grant of stock options*, I may further conclude that those options were not granted consistent with a fiduciary’s duty of utmost loyalty.¹²⁴

Thus, a spring-loading breach of duty claim maintained in the absence of non-compliance with a shareholder-approved option plan must nevertheless include affirmative deception of the shareholders or half-truths about the option grants, something more than the grant of the options on favorable terms informed by material nonpublic information known to the persons who made the grant.

123. *Tyson*, 919 A.2d at 575. One commentator noted that this case suggests that “absent an agreed-upon plan between executives and shareholders such as the one present in Tyson Foods, it appears that spring-loading may withstand the test of the business judgment rule.” Jonathan J. Tompkins, Note, *Opportunity Knocks, but the SEC Answers: Examining the Manipulation of Stock Options Through the Spring-Loading of Grants and Rule 10b-5*, 26 WASH. U. J.L. & POL’Y 413, 449–50 (2008). This was, however, written without reference to the later opinion in *Tyson*, discussed at *infra* text accompanying note 124.

124. *In re Tyson Foods, Inc.*, Civ. A. No. 1106-CC, 2007 WL 2351071, at *4–5 (Del. Ch. Aug. 15, 2007) (emphasis added). As stated at *supra* note 122, the case was settled.

“Bullet-dodging,” referred to by the *Tyson* court,¹²⁵ occurs when the board delays granting the option until adverse nonpublic material information known to the board is disclosed, thereby causing a reduction in the market price and, correspondingly, in the option exercise price set at the time of the grant.¹²⁶ In a leading case the court observed:

I am skeptical that a bare allegation that a board of directors made a discretionary issuance of stock options at the market stock price after releasing negative information can ever be sufficient in itself to state a claim of director disloyalty, even when a stockholder-approved option plan requires fair-market-value grants,¹²⁷

As the court observed in summarizing its ruling:

Although stockholders might quibble with the decision whether to give large slugs of options to officers after a disappointing quarter, *no deception on the stockholders, the market, or regulatory authorities is involved* and the officers have the intended incentive to perform well in order to help the corporation’s stock price improve from its level on the date of issuance, a level that reflects the negative information released.¹²⁸

Thus, affirmative deception of the stockholders is an element of a breach of duty claim for bullet-dodging when granting stock options; the well-timed delayed grant alone, informed as the decision to delay was by nonpublic information, is not sufficient to state a cause of action.

A later case confirmed that deception of stockholders is an element of the breach in both the spring-loading and bullet-dodging context.¹²⁹

Taking Weiss’s allegations in this case as true, it is reasonable to infer that stockholders would consider the practice of timing options described in the complaint to be important in deciding whether to approve the option plans or to reelect board members. In other words, the well-pleaded allegations in the complaint support an inference that the Director Defendants’ alleged practice of granting spring-loaded and bullet-dodged options *in conjunction with earnings releases* was material information. Under *Tyson*, because the allegations of the complaint support an inference that the Director Defendants never disclosed this practice in the plans themselves, subsequent proxy statements, or SEC filings describing the option grants, the allegations in the complaint also give rise to an inference that the Director Defendants, in violation of their fiduciary duties, intended to circumvent the restrictions found in the plans.¹³⁰

In the Plan disclosure timing context, by contrast, there has been no shareholder approved scheme for creating and implementing Plans that could be

125. See *supra* text accompanying note 122.

126. *Desimone v. Barrows*, 924 A.2d 908, 918 (Del. Ch. 2007). This decision was rendered between the first and second *Tyson* decisions.

127. *Id.* at 944.

128. *Desimone*, 924 A.2d at 916 (emphasis added).

129. *Weiss v. Swanson*, 948 A.2d 433, 441–48 (Del. Ch. 2008) (denying motion to dismiss, where court found claim stated for breach of fiduciary duty for spring-loading and bullet-dodging). This case was also settled. *Weiss v. Bell*, No. 2828-VCL, 2011 WL 1630821 (Del. Ch. Apr. 28, 2011).

130. *Weiss*, 948 A.2d at 443 (emphasis added) (footnote omitted).

breached or disregarded. There are, at least in most cases, no representations to the shareholders regarding the administration of the Plans, and no enrichment of the executive *at the actual or alleged expense of the corporation* (as there is in spring-loading or bullet-dodging), that is, no cost to the company comparable to using material nonpublic information to decide when to grant options in order to provide an exercise price that benefits grantees and may thus under-compensate the company when the option is exercised.

Weiss suggests that spring-loading or bullet-dodging practices are material information in the context of the annual proxy statement distributed in connection with the election of directors. That is, disclosure of these practices is material to the decision on voting for a director candidate. If, however, the directors themselves are unaware of any disclosure timing in connection with the implementation of Rule 10b5-1 Plans, the fact that non-director executives engaged in disclosure timing is likely not material to the decision of a shareholder in deciding whether to vote for the reelection of that uninformed director.¹³¹ Thus, nothing in the Delaware law regarding breach of the duty of loyalty in granting options reaches executive disclosure timing to produce better outcomes under Rule 10b5-1 Plans.¹³²

D. THE CORPORATE OPPORTUNITY DOCTRINE

Another possible avenue of inquiry is the familiar corporate opportunity doctrine. The doctrine

holds that a corporate officer or director may not take a business opportunity for his own if: (1) the corporation is financially able to exploit the opportunity; (2) the opportunity is within the corporation's line of business; (3) the corporation has an in-

131. A fact omitted from a proxy statement is material only "if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976). It is unlikely that it would be material that a director failed to take any action about something he did not know about. One case decided soon after *TSC Industries* agreed with defendants' contention that "[n]o case has . . . held that the proxy rules are violated because management has allegedly mismanaged the company, and the proxy statement does not say so." *Markewich v. Adikes*, 422 F. Supp. 1144, 1147 (E.D.N.Y. 1976). *Markewich* was cited with approval in *Bank & Trust Co. of Old York Road v. Hankin*, 522 F. Supp. 1330, 1335–36 (E.D. Pa. 1982), where the court stated that non-disclosure of "misconduct which is little more than the breach of a fiduciary duty or the waste of corporate assets" is "never material" under Rule 14a-9. To be sure, in the end questions of materiality are very fact specific. *TSC Indus.*, 426 U.S. at 450.

A claim that the directors failed to oversee officers presents an extremely high bar of allegations and proof. See *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (holding that a claim against directors for failure to supervise lies only if "(a) the directors utterly failed to implement any reporting or information system or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention"). Thus, an allegation that a proxy statement was materially false for failing to describe the directors' breach of duty in failing to supervise an officer who engaged in disclosure timing for his own benefit seems highly unlikely to succeed.

132. As the discussion in the text reflects, the option grant cases arose like a volcano erupting. The leading cases were settled, however, and so the law did not develop beyond the pleadings stage. One cannot predict what course the law might take if another similar spate of misbehavior emerged, though a recent study presents evidence that the practices continue. See Avci et al., *supra* note 52, at 3, 6, 10–22.

terest or expectancy in the opportunity; and (4) by taking the opportunity for his own, the corporate fiduciary will thereby be placed in a position inimicable to his duties to the corporation.¹³³

Plan disclosure timing does not fall within that framework. Most significantly, the corporation itself cannot benefit from using this corporate information in a securities transaction, albeit if the company itself has a repurchase Plan in place the transactions could proceed lawfully, at least under federal law. That is, as noted above under Scenario C,¹³⁴ corporate trading for the corporation's own account is constrained by the classical theory of insider trading under Rule 10b-5.¹³⁵ Thus, the information known to the executive that he uses to engage in disclosure timing is not something the corporation could affirmatively use for its own benefit absent the corporation's own Plan. If both the company and the executive had Plans for their respective trading in the company's stock (a repurchase program in the case of the company), both could engage in disclosure timing without violating Rule 10b-5. However, both may be subject to the common law of insider trading, as discussed in the next part.

E. THE COMMON LAW OF INSIDER TRADING¹³⁶

Because the scenarios presented at the beginning of this article¹³⁷ entail using nonpublic corporate information to achieve a more favorable outcome in trading company stock, the closest state law parallel may be the common law that addresses whether a corporation, or a shareholder suing derivatively on behalf of the company, has a cause of action to recover profits realized by an insider who has traded in company stock using material nonpublic information.

Delaware has long recognized a common law cause of action for insider trading. In the seminal case *Brophy v. Cities Service Co.*,¹³⁸ Kennedy, a confidential secretary of a director and officer of the company, knew that the company was going to repurchase its stock in the market. In advance of those transactions Kennedy bought company stock. He sold it at a profit after the company made its purchases, which had moved the market price up.¹³⁹ The court found that Kennedy, though neither a director nor an officer, nevertheless occupied a position of trust and confidence analogous to that of a fiduciary and as such could not use nonpublic corporate information for a purchase "for his own personal gain."¹⁴⁰ The fact that there was no alleged loss to the corporation was not a fatal defect in the claim¹⁴¹:

133. *Broz v. Cellular Info. Sys., Inc.*, 673 A.2d 148, 154–55 (Del. 1996).

134. See *supra* text accompanying notes 16–17.

135. See *supra* note 15.

136. This article does not seek to present a comprehensive review of the state common law of recovery of insider trading profits by the corporation, only to reflect the principal lines of authority.

137. See *supra* text following note 12.

138. 70 A.2d 5 (Del. 1949).

139. *Id.* at 7.

140. *Id.* at 8.

141. The court did not address whether Kennedy's purchases moved the market price up, increasing the cost to the company of its later purchases, thereby damaging the company in its repurchase

In equity, when the breach of a confidential relation by an employee is relied on and an accounting for any resulting profits is sought, loss to the corporation need not be charged in the complaint. Public policy will not permit an employee occupying a position of trust and confidence toward his employer to abuse that relation to his own profit, regardless of whether his employer suffers a loss.¹⁴²

He would therefore have to account to the corporation for his profit if the allegations were proven.¹⁴³

The *Brophy* claim is still recognized in Delaware,¹⁴⁴ as it is in New York:

[A] person who acquires special knowledge or information by virtue of a confidential or fiduciary relationship with another is not free to exploit that knowledge or information for his own personal benefit but must account to his principal for any profits derived therefrom. This, in turn, is merely a corollary of the broader principle, inherent in the nature of the fiduciary relationship, that prohibits a trustee or agent from extracting secret profits from his position of trust.¹⁴⁵

New Jersey recognizes the cause of action where the plaintiff establishes that the corporation was harmed by the insider's actions.¹⁴⁶

Other jurisdictions have declined to follow *Brophy*, in whole or in part. Florida rejected the cause of action, at least in the absence of damage to the corporation.¹⁴⁷ The ruling addressed a derivative claim to recover profits from a tippee of an insider of the corporation on whose behalf the claim was brought. Because the outsider-tippee owed no duty to the corporation the court rejected an "unprecedented expansive reading" of *Diamond* to hold him liable to the corporation.¹⁴⁸ The court went on to reject the "innovative ruling" of *Diamond* itself had the claim been made against insiders who did owe fiduciary duties to the corporation.¹⁴⁹

program. The court stated only, "[l]oss or damage to the corporation cannot be inferred from these general and indefinite allegations." *Id.*

142. *Id.*

143. *Id.*

144. See *Kahn v. Kolberg Kravis Roberts & Co.*, 23 A.3d 831, 836–40 (Del. 2011) (adhering to *Brophy*, "it is inequitable to permit the fiduciary to profit from using confidential corporate information. Even if the corporation did not suffer actual harm, equity requires disgorgement of that profit . . .").

145. *Diamond v. Oreamuno*, 248 N.E.2d 910, 912 (N.Y. 1969). The court held that the plaintiff's failure to allege that the corporation was damaged was not a fatal omission. *Id.* at 912. The court did observe, however, that "it may well be inferred that the defendants' actions might have caused some harm to the enterprise [which] has a great interest in maintaining a reputation of integrity, an image of probity, for its management and in insuring the continued public acceptance and marketability of its stock." *Id.*

146. *In re ORFA Sec. Litig.*, 654 F. Supp. 1449, 1458 (D.N.J. 1987); see also *Frankel v. Slotkin*, 984 F.2d 1328, 1336–37 (3d Cir. 1993) (following *ORFA*, granting summary judgment for the defendant because the plaintiff had failed to adduce evidence of harm to the company).

147. *Schein v. Chasen*, 313 So. 2d 739, 746–47 (Fla. 1975). The case was decided on certification of a legal question from the U.S. Court of Appeals of the Second Circuit on remand from the Supreme Court.

148. *Id.* at 745–46.

149. *Id.* at 746 (quoting with approval dissenting opinion of Judge Kaufman in an earlier decision in the case, *Schein v. Chasen*, 478 F.2d 817, 828 (2d Cir. 1973), *vacated & remanded*, 416 U.S. 386 (1974)).

The U.S. Court of Appeals for the Seventh Circuit, ruling in the absence of Indiana law directly on point,¹⁵⁰ held that under Indiana law the *Brophy/Diamond* cause of action would be rejected altogether.¹⁵¹ A federal court, following *Freeman*, held that the courts of the State of Washington would not follow *Brophy* and even if there were such a common law cause of action damage to the corporation would be an essential element.¹⁵² Without supporting citation, one court held that Ohio law does not recognize a derivative cause of action for insider trading.¹⁵³ California has created a cause of action by statute.¹⁵⁴

Brophy and its progeny condemn use of a corporate asset, information, to personally benefit in a securities transaction. If damage is an essential element of such a breach of duty claim, there would be no liability in any of the Plan-related disclosure timing scenarios posited here. At most, there may be some damage to the reputation of the corporation,¹⁵⁵ and it is questionable that a court would award damages in such a case.¹⁵⁶

If damage is not an essential element of the cause of action for breach of duty, then use of corporate information to engage in disclosure timing that achieves a more favorable outcome of a Plan transaction may be a breach of duty. Parallel to the measure of recovery in cases such as *Brophy*,¹⁵⁷ the recovery would be the incremental benefit achieved (additional profit or loss avoided) by the use of nonpublic corporate information. This would be similar but not identical to what courts are called upon to do when imposing orders of disgorgement and penalties for insider trading under section 21A of the Exchange Act.¹⁵⁸

150. *Freeman v. Decio*, 584 F.2d 186, 188 (7th Cir. 1978).

151. *Id.* at 196 (“Although the question is a close one, we believe that were the issue to be presented to the Indiana courts at the present time, they would most likely join the Florida Supreme Court in refusing to adopt the New York court’s innovative ruling [in *Diamond*].”).

152. *In re Cray Inc. Derivative Litig.*, 431 F. Supp. 2d 1114, 1132–33 (W.D. Wash. 2006).

153. *In re Goodyear Tire & Rubber Co. Derivative Litig.*, Nos. 5:03CV2180 et al., 2007 WL 43557, at *8 (N.D. Ohio Jan. 5, 2007).

154. CAL. CORP. CODE §§ 25402, 25502.5 (West 2006). The cause of action is available only with respect to securities transactions within the state (§ 25402) and in respect of securities of companies with total assets in excess of one million dollars and a class of equity security held of record by 500 or more persons (§ 25502.5(d)). Any recovery is offset by any amount paid by the defendant in a proceeding brought by the SEC obtaining sanctions for insider trading. § 25502.5(b). See *Friese v. Superior Court of San Diego Cty.*, 134 Cal. App. 4th 693 (2006) (upholding application of the provisions to a corporation organized under a law other than that of California, and rejecting argument that internal affairs doctrine applies to trading in the securities of foreign corporations). There have been no reported cases of a recovery based on these provisions. California has adopted the affirmative defenses in Rule 10b5-1. See CAL. CODE REGS. tit. 10, § 206.402 (2016).

155. See *supra* note 145 (noting mention in *Diamond* of possible damage to corporate reputation albeit damage is not an element of the cause of action under New York law).

156. See *In re Shawe & Elting LLC*, C.A. No. 9661-CB, 2015 WL 4874733, at *28 (Del. Ch. Aug. 13, 2015) (noting that in the corporate context irreparable injury exists when monetary damages would be speculative, which includes the situation where the corporation has allegedly suffered injury to its reputation), *appeal refused*, 2015 WL 5720403 (Del. Sept. 28, 2015).

157. See *supra* text accompanying notes 141–43.

158. 15 U.S.C. § 78u-1 (2012); see *LANGEOORT*, *supra* note 9, § 8:11 (describing the principles applied in calculating disgorgement in an SEC action based on unlawful insider trading); *id.* § 8:2 (describing the method for calculating a penalty based on profits gained or losses avoided, as prescribed by section 21A(a)(2)).

When disgorgement is addressed in an insider trading case where the gravamen was the purchase of stock based on material nonpublic information, “[once] a fraudulent buyer has reached the point of his full gain from the fraud, viz., the market price a reasonable time after the undisclosed information has become public, any consequence of a subsequent decision, be it to sell or to retain the stock, is *res inter alios*, not causally related to the fraud.”¹⁵⁹ This calculation is based on the movement of the stock price after actual disclosure of the previously undisclosed information, an event that is easy to identify. In the case of disclosure timing, however, the assessment of the profit gained depends on a determination of what the market price would have been had the corporate disclosure been made at some earlier time, when the corporation *would have* disclosed the information *but for* the executive’s interference with the disclosure process. This determination has a hypothetical component that may be more difficult to establish.

Nevertheless, while it may be difficult to determine after the fact when public disclosure *would have been made* in the absence of the executive’s interference with the disclosure process, and thus what any benefit was to the executive may have an element of speculation, that uncertainty should not preclude a damage recovery by or on behalf of the company:

One to whom another has tortiously caused harm is entitled to compensatory damages for the harm if, but only if, he establishes by proof the extent of the harm and the amount of money representing adequate compensation *with as much certainty as the nature of the tort and the circumstances permit*.¹⁶⁰

At the same time:

It is desirable . . . that there be definiteness of proof of the amount of damage as far as is reasonably possible. It is even more desirable, however, that an injured person not be deprived of substantial compensation merely because he cannot prove with complete certainty the extent of harm he has suffered.¹⁶¹

In any case, the executive has not caused the corporation to violate the securities laws, exposing it to enforcement sanctions or a private civil damage recovery, such as by failing to make a disclosure by a deadline imposed by some SEC rule or making an affirmative materially false public statement, as in the option backdating cases.¹⁶² Thus, the executive is at most exposed to a recovery of his own increased profits or reduced losses in a jurisdiction where the use of material nonpublic information in a securities transaction is a breach of duty in the absence of damage to the corporation.¹⁶³

159. SEC v. McDonald, 699 F.2d 47, 54 (1st Cir. 1983), discussed in LANGEVOORT, *supra* note 9, § 8:11.

160. RESTATEMENT (SECOND) OF TORTS § 912 (AM. LAW INST. 1979) (emphasis added).

161. *Id.* cmt. A.

162. See *supra* text accompanying note 115.

163. Because the claim would be one for breach of loyalty, any exculpation clause in the corporate charter would not preclude a damages recovery. See DEL. CODE ANN. tit. 8, § 102(b)(7) (2013) (providing that the charter of a Delaware corporation may include a provision eliminating the personal

V. THE USE OF CORPORATE INFORMATION IN DECIDING TO CANCEL A PLAN IS NOT A BREACH OF DUTY

A related issue in the common law context is whether the use of nonpublic corporate information to make a decision to *cancel* a Plan, where the executive does *not* alter the timing of disclosure of the information, is a breach of duty.¹⁶⁴ In that situation the executive avoids a Plan sale before market-increasing information is released or avoids a Plan purchase before market-depressing information is released. No investor is harmed in those situations, because any corporate disclosure was made in due course as required by law and the executive did not engage in a transaction with anyone. As a general rule, a corporate executive may use material nonpublic corporate information when the use is “not in connection with trading of the corporation’s securities, is not a use of proprietary information of the corporation, and does not harm the corporation.”¹⁶⁵ The cancellation of a trade is not “in connection with trading of the corporation’s securities.”¹⁶⁶ There thus is no basis to require the executive to account to the corporation for the savings he achieved by aborting a transaction.

VI. STATE ENFORCEMENT AUTHORITIES ARE NOT LIKELY TO TAKE ACTION TO OBTAIN SANCTIONS FOR MERE BREACHES OF FIDUCIARY DUTY

If there were a breach of a common law fiduciary duty, it is doubtful that either state or federal governmental authorities have any power to prosecute this conduct in civil or criminal enforcement matters, because the behavior is not within a statutory violation such as embezzlement, misapplication of corporate funds, or mail fraud. There is no authority to bring an action for a mere breach of fiduciary duty.¹⁶⁷ One searches corporate law texts in vain for any hint that regulators or law enforcement officials, such as secretaries of state or attorneys general, have any statutory power to pursue remedies for corporate law breaches of duty. It is apparent that legislatures have deferred to the plethora of private remedies available to the corporations themselves, to shareholders, and to cred-

liability of a director for monetary damages for breach of fiduciary duty, “provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director’s duty of loyalty to the corporation or its stockholders”).

164. As noted earlier at *supra* text accompanying notes 43–44, it is not a violation of Rule 10b-5 to use material nonpublic information in deciding to cancel a Plan.

165. 1 PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 5.04(a)(3) (AM. LAW INST. 1994).

166. See *supra* text accompanying notes 43–44 (stating SEC Staff position that cancellation of trade is not proscribed by Rule 10b-5 because it is not “in connection with the purchase or sale of a security”). Nothing in the source cited at *supra* note 165 suggests that the common law meaning of the concept is broader.

167. Renee M. Jones & Michelle Welsh, *Toward a Public Enforcement Model for Directors’ Duty of Oversight*, 45 VAND. J. TRANS’L L. 343, 390 (2012) (proposing adopting Australian approach to public enforcement of director misconduct, noting that “[u]nder state corporate laws . . . there are no provisions for public enforcement of fiduciary duties”); see also Megan W. Shaner, *The (Un)Enforcement of Corporate Officers’ Duties*, 48 U.C. DAVIS L. REV. 271 (2014) (proposing improvements to enforcement of fiduciary duties with no reference to existing or proposed state governmental enforcement).

itors to hold to account any officer who breaches a duty that is not a violation of a general criminal prohibition. Given the other avenues for relief, it is not surprising that authorities at the state level have not demonstrated a taste for seeking to vindicate state corporate law duties.¹⁶⁸

VII. CONCLUSION

If an insider who trades pursuant to a Rule 10b5-1 plan monitors the way the Plan works so that he knows when a transaction will or may occur under the Plan, his action to cause or to influence a delay of public disclosure of material information about the company, when that delay does not violate a mandatory time-based disclosure requirement under the SEC's Exchange Act rules, does not violate Rule 10b-5 or any other provision of the federal securities laws. Nor could a rule be adopted by the SEC under current law to render this conduct unlawful. New legislation would be needed if the SEC were to have the authority to prohibit Plan-related disclosure timing.

Two steps could be taken under present legislative authority. One is to require Plan-related disclosures under the powers granted the SEC to require disclosure by public companies and persons trading in the markets.¹⁶⁹ The other is to exclude disclosure-timers from the protections afforded by Rule 10b5-1.¹⁷⁰

A review of state corporate law, with a focus on the law of Delaware, suggests a limited basis for finding that an executive's disclosure timing activity is an actionable breach of duty by an officer or director of the corporation, with damages calculated in a manner comparable to, though potentially more complex than, the remedy of disgorgement commonly applied in SEC enforcement actions for unlawful insider trading.

168. See Mark J. Roe, *Delaware's Politics*, 118 HARV. L. REV. 2491, 2501 (2005) ("No Delaware prosecutor scrutinizes corporate America to throw wrongdoers in jail; it could build a prosecutorial office or a regulatory agency to empower other interests or ideas, but it hasn't.").

169. See *supra* text accompanying notes 89–98.

170. See *supra* text accompanying notes 99–101.