

## SIGNIFICANT CHANGES IN WHAT AND WHEN INSIDERS NEED TO REPORT UNDER SECTION 16(A) OF THE '34 ACT

The Securities and Exchange Commission ("SEC") has adopted new rules under Section 16(a) of the Securities Exchange Act of 1934, as amended, requiring insiders of public companies to report changes in beneficial ownership *in as little as two business days*. This newsletter summarizes these reporting requirements as now in effect.

**Background.** The rules were promulgated pursuant to the Sarbanes-Oxley Act of 2002, which contains a variety of highly publicized new requirements for public companies, such as officer certification of periodic reports. Less publicized, but of immediate significance, are its amendments to Section 16(a) of the Exchange Act to require insiders—directors, officers and 10% shareholders—of publicly traded companies to report any transaction resulting in a change in beneficial ownership of company stock within two business days of the transaction, except in those instances where the SEC determines that this deadline would not be feasible or appropriate.

The new rules were effective immediately and have an impact to anyone who is an officer, director or 10% shareholder of a publicly-traded company. *The new rules significantly expand the list of transactions which must be reported on Form 4 and dramatically accelerate the time period in which such reports must be filed.* The prior rule gave insiders until 10 days after the end of the month in which the transaction occurred to file (in some cases up to 40 days after the transaction).

**Accelerated Disclosure.** Section 16(a) now requires insiders of public companies to file on Form 4 with the SEC within two business days of the date of the transaction changing the person's beneficial ownership in the company. The "date of the transaction" generally means the date the transaction is executed. The Form 4 must disclose the beneficial ownership of the insider at the date of filing, and the changes in beneficial ownership and purchases and sales of security-based swap agreements that occurred since the most recent filing.

**Limited Deadline Extension.** The new rules provide for only two limited exceptions to the strict two business day filing deadline. In both cases the insider does not control and may not know in advance the timing of the transaction:

- Certain transactions pursuant to Rule 10b5-1(c) plans where the terms of the plan are such that the insider does not select the date of execution.
- "Discretionary transactions" under employee benefit plans where the insider does not select the date of execution, such as intra-plan fund transfers.

For these transactions, the deemed "date of execution" will be the date on which the insider is notified of the execution, *but not later than the third business day after the actual trade date*. Effectively, this provides a maximum of five business days for these transactions to be reported—three business days for the insider to be notified by the broker or plan administrator and two business days for the insider to report the transaction.

**Form 4 Reporting Required for Additional Transactions.** In addition to the accelerated filing deadlines for trading transactions, many transactions previously reportable on Form 5 on a deferred basis annually are now subject to the two business day reporting rule and must be reported on Form 4, including:

- Grants, awards and other acquisitions from the issuer, such as the grant of stock options or restricted stock awards.
- Dispositions of equity securities to the issuer, such as a sale of shares to the company or the cancellation of options in an option repricing or exchange program.
- Certain "discretionary transactions" under employee benefit plans. Generally, these are voluntary transactions under a company retirement plan involving an intra-plan transfer into or out of a company stock fund or a cash distribution funded by a disposition of securities in a company stock fund.
- Certain "small acquisitions" if they are made from the issuer or an employee benefit plan sponsored by the issuer. Previously reportable on Form 5, these "small acquisitions" are acquisitions not exceeding \$10,000 in the aggregate during a six-month period which meet certain additional conditions. Note that small acquisitions from an entity other than the issuer remain reportable on Form 5.

**Exempt Transactions.** Certain transactions previously exempt from Section 16(a) reporting remain exempt under the new rules. These include the following:

- Stock splits, stock dividends and pro rata rights issued under stockholder rights plans or preemptive rights;
- Acquisitions resulting from the reinvestment of dividends or interest pursuant to broad-based dividend or interest reinvestment plans;
- Non-discretionary transactions under tax conditioned plans (i.e. qualified plans, excess benefit plans and employee stock purchase plans); and
- Transactions which merely change the form of beneficial ownership of the equity securities, other than the exercise or conversion of derivative securities, such as the transfer of securities out of an employee benefit plan to direct beneficial ownership.

**Penalties.** Any late Form 4 filings must be disclosed in the proxy statement and a box must be checked on the cover page of the issuer’s Form 10-K indicating that late filings were made. Additionally, the Sarbanes-Oxley Act gives the SEC broad authority to seek any equitable relief it

finds appropriate or necessary to benefit investors for any violations of the new two business day filing deadline.

**Compliance Recommendations.** If they have not already done so, issuers should immediately inform their directors and executive officers of these reporting changes. Directors and officers should coordinate with their brokers to insure timely compliance. In addition, issuers should evaluate their equity grant procedures to ensure compliance with the two business day reporting requirements. To the extent that an issuer’s reporting officers or directors receive equity grants, advance preparation will be necessary to avoid inadvertent filing delays since the grant by the Compensation Committee, if effective immediately as is usually the case, will need to be reported within two business days. Also, the Sarbanes-Oxley Act requires that Section 16 reports be filed on EDGAR beginning July 30, 2003. Accordingly, all directors and executive officers should make plans to file via EDGAR, including obtaining SEC CIK/CCC numbers.

If you have any questions or would like additional information on the accelerated reporting deadlines, please contact **Barbara A. Young, Peter H. Struzzi** or **Kristine M. Murphy** of our office at **203-222-0885**.

**Summary of Requirements of Forms 3, 4 and 5.** Below is a chart summarizing requirements of Forms 3, 4 and 5. Each of the forms generally requires the name of the insider, title, type of transaction, date of the transaction, amount of stock acquired or disposed, price, holdings after the transaction and the nature of ownership. A copy of the form must be sent to each exchange on which shares of the issuer are traded and the issuer (either a designated person, or if none designated, the issuer’s corporate secretary) no later than when transmitted to the SEC for filing.

Form	Form Type	Summary of Requirements
Form 3	Initial Statement of Beneficial Ownership of Securities	This form must be filed within 10 days after becoming a director, officer or 10% or more holder of the outstanding shares of a public company’s stock. For example, a 5% owner, upon attaining the 10% level of ownership, would be required to file a Form 3. This form is filed only once by an insider for each company.
Form 4	Statement of Changes of Beneficial Ownership of Securities	This form is required any time there is a change in an insider’s beneficial ownership—for example, by an open market purchase or sale, or an acquisition, exercise or conversion of options or derivative securities (e.g. puts, calls). It must be filed by the end of the 2 <sup>nd</sup> business day following the transaction.
Form 5	Annual Statement of Beneficial Ownership of Securities	This form must be filed annually within 45 days after the close of the issuer’s fiscal year to disclose transactions exempt from prior reporting, as well as transactions that should have been reported previously on Form 3 or Form 4, but were not. End of the year reporting on Form 5 continues to be available for the following types of transactions: (i) bona fide gifts; (ii) transfers of securities by will or inheritance; and (iii) acquisitions of equity securities (other than from the issuer) of less than \$10,000. A Form 5 is not necessary if there have not been any transactions to report.

Note that when a director retires or exits from the company, he or she should check the “exit” box on Form 4 or Form 5. The individual is required to continue reporting transactions occurring within six months after retiring or exiting.

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