



**FENWICK & WEST LLP**

*CORPORATE & SECURITIES LAW UPDATE*

## New Rules Requiring Two-Day Filing of Forms 4 Are In Effect

August 29, 2002



## New Rules Requiring Two-Day Filing of Forms 4 Are In Effect

On August 29, 2002, new rules went into effect requiring officers, directors and greater than 10% stockholders of public companies to file Forms 4 with the SEC within two days of most transactions in company securities. These rules were mandated by the Sarbanes-Oxley Act of 2002 and were adopted by the SEC on August 27, 2002. The complete text of the rules can be found at: <http://www.sec.gov/rules/final/34-46421.htm>.

The SEC also adopted final rules requiring accelerated filing, and web site posting, of Forms 10-K and 10-Q and requiring new CEO and CFO certifications to be filed with Forms 10-K and 10-Q as mandated by Section 302 of the Sarbanes-Oxley Act. We will distribute separate updates addressing these rules once the SEC makes the rules available.

### What is the new Form 4 deadline?

For most transactions in company securities, insiders will need to file a Form 4 with the SEC by the end of the second business day following the transaction. The Form 4 must be received by the SEC no later than 5:30 p.m. Eastern time (2:30 p.m. Pacific time) on the due date. For example, if a reportable transaction occurs on Monday at 11:00 a.m., the Form 4 reflecting the transaction will be due Wednesday by 5:30 p.m. Eastern time.

For a few transactions for which a Form 4 is required, the SEC has provided limited additional time for insiders to file their Forms 4. The deadlines for these Form 4 transactions are as follows:

Type of Transaction	Form 4 Deadline
Rule 10b5-1(c) plan transactions, where the insider does not select the date of execution	Within two business days after date of notification of trade by broker, dealer or plan administrator, but the notification must be made within three business days after the trade (or it will be deemed made as of that deadline)
Discretionary transactions under certain employee benefit plans, where the insider does not select the date of execution	Within two business days after date of notification of trade by the plan administrator, but the notification must be made within three business days after the trade (or it will be deemed made as of that deadline)

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### **Have the deadlines for filing Forms 3 or Forms 5 changed?**

No. Forms 3 are still due within 10 days after becoming an officer, director or greater than 10% stockholder of a public company (or upon the effectiveness of the company's 1934 Act registration statement in connection with an IPO). If an insider is required to file a Form 4 before the Form 3 is due (for example, because the insider received a stock option grant upon becoming an insider), then the SEC has encouraged the insider to file the Form 3 along with the Form 4 at the time the Form 4 is due.

Forms 5 are still due within 45 days after the end of the company's fiscal year.

### **What must be reported on a Form 4?**

Insiders must now report on Form 4:

- all transactions that are not exempt from the short-swing profit recovery requirements of Section 16(b);
- all transactions between the insider and the company that are exempt from Section 16(b) pursuant to Rules 16b-3(d), (e) and (f); and
- all exercises and conversions of derivative securities.

The primary difference between the new rules and prior requirements is the need to file on Form 4 (rather than on Form 5) transactions in the second category, which include stock option grants, restricted stock awards, issuer stock repurchases and "discretionary transactions" under employee benefit plans. These changes do not alter the treatment of elections to participate in, and routine purchases under, employee stock purchase plans, 401(k) plans and certain other ERISA plans, which continue to be exempt from Section 16 reporting altogether.

Reportable securities include any class of the company's equity securities and any derivative security, as well as security-based swap agreements and security futures products relating to those securities. Insiders are required to report securities in which they have a direct or indirect pecuniary interest. Therefore, insiders may be required to report transactions by other individuals, entities or trusts, if the insider has a pecuniary interest in the securities held by those persons.

The following transactions are among those that will now need to be reported on a Form 4:

- most purchases and sales of securities for value, including:
  - open market purchases and sales;
  - private purchases and sales;
  - acquisitions from or dispositions to the company;

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- acquisitions or dispositions of company securities in connection with an acquisition transaction between the company and another entity; and
  - acceptance of tendered securities by a party making a tender offer for the company’s securities;
  - stock option grants, stock bonus awards, restricted stock awards and acquisitions of most other rights to purchase the company’s securities;
  - exercises of options, warrants and other derivative securities and conversions of derivative securities;
  - vesting of performance-based awards (where performance conditions are not tied to either market price or passage of time and continued employment);
  - “discretionary transactions” under employee benefits plans (for example, an intra-plan transfer of previously invested assets into or out of a company securities fund maintained under the plan, or cash-outs from a company securities fund maintained under the plan);
  - repricings of outstanding options;
  - any other transaction where a put or call equivalent position is established, increased, decreased, exercised or converted;
  - cancellations or expirations of put or call equivalent positions, unless they involve long derivative security positions and no value is received for the cancellation or expiration;
  - entry into, change in position under, termination of and settlement of, hedging transactions (such as zero-cost collars and equity swaps);
  - receipt of securities in a partnership or LLC distribution, where the insider was not deemed to be the beneficial owner of these securities before the distribution (and therefore had not previously reported them); and
  - distributions of securities by partnerships or corporations that are reporting insiders (such as distributions by greater than 10% stockholders or members of a group that holds greater than 10%).

Form 4 reporting requirements can be complicated, and Form 4 reporting can be required for many transactions that do not at first glance appear to be acquisitions or dispositions of securities. ***Therefore, insiders should confer with the company’s compliance officer before engaging in any transaction that relates to company securities to allow sufficient time to determine the appropriate reporting position and complete the required filing within the accelerated filing deadline.***

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**Has the format of the Form 4 that must be filed with the SEC changed as a result of the new rules?**

Yes. The SEC is revising the format of the Form 4, including the following:

- The existing Form 4 will be revised to make clear that the “holdings” columns (column 5 of Table I and column 9 of Table II) should include the insider’s securities holdings following the reported transactions, rather than month-end holdings; and
- A new column 2A will be added to Table I and a new column 3A will be added to Table II of the Form 4. These new columns will report the date the insider was notified of transactions that qualify for deferred Form 4 reporting (i.e., Rule 10b5-1(c) plan transactions or discretionary transactions under an employee benefit plan, where the insider did not select the date of execution) and will enable the SEC and investors to determine if the Form 4 was filed on a timely basis.

The SEC plans to publish a new Form 4 with these changes as soon as it can. Until then, insiders should continue to use the versions that are currently available, but should modify box 4 (“Statement for Month/Year”) to state the month, day and year of the transaction. In addition, we recommend that, since the insider’s aggregate holdings in column 5 of Table I and column 9 of Table II are being presented immediately following the transaction being reported, the insider should make a footnote reference to that effect. The SEC has also indicated that, until it publishes the new Form 4, insiders should also put an asterisk next to the trade date in the transaction date column (column 2) and footnote the deemed execution date for transactions that qualify for delayed Form 4 reporting.

**What can still be reported on a Form 5?**

The following transactions can still be reported by an insider on a Form 5 within 45 days of the end of the company’s fiscal year:

- gifts;
- transfers by will or the laws of descent;
- most deposits into and withdrawals from voting trusts; and
- certain small acquisitions (not exceeding \$10,000 in market value, provided that the securities are not acquired from the company and the insider has not made other non-exempt, unreported acquisitions within the prior six months that would, together with this acquisition, exceed the \$10,000 threshold and does not make any non-exempt disposition within the ensuing six months).

However, these transactions can be voluntarily reported on a Form 4 in advance of the Form 5 deadline.

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**Are there any transactions that are still not required to be reported on a Form 4 or a Form 5?**

Yes. Many transactions and events, including those listed below, remain exempt from Section 16 reporting (no Form 4 or Form 5 reporting is required):

- a change in the form of beneficial ownership without changing the insider's pecuniary interest in the securities (except exercises or conversions of derivative securities and deposits or withdrawals from voting trusts);
- transactions (other than "discretionary transactions") under ESPP and 401(k) plans (for example, elections to participate in, and routine purchases of shares from the company under, these plans);
- vesting of shares under a nonperformance-based option;
- expiration or cancellation of a derivative security representing a long derivative security position, if no value is received in connection with the transaction;
- certain distributions of a substantial block of securities by persons engaged in the business of distributing securities;
- stock splits and stock dividends that apply equally to all securities of a class;
- acquisitions of securities from the reinvestment of dividends or interest on securities if the acquisition is made under a broad-based, non-discriminatory plan providing for the regular reinvestment of dividends or interest; and
- the acquisition or disposition of securities pursuant to a domestic relations order.

As indicated above, these transactions are not separately reportable. However, any securities that are acquired or disposed of pursuant to these transactions should be reflected in the "holdings" column of the next Form 4 or Form 5 that is filed by an insider, with a footnote explaining the change in number of shares from the previously filed report.

As discussed above, the Section 16 reporting requirements can be complicated. Therefore, insiders should confer with the company's compliance officer before engaging in any transaction that relates to company securities to allow sufficient time to determine the appropriate reporting position.

**Do the new rules change the short-swing profit recovery rules under Section 16(b)?**

No. The new rules change Section 16(a) reporting requirements. Section 16(b) continues to require that insiders reimburse the company if, within any six-month period, the insider profits from any purchase and sale (or sale and purchase) of securities that are not exempt from Section 16(b). Given the complex nature of the Section 16(b) rules, insiders should confer with the company's compliance officer before engaging in any transaction that

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relates to company securities, in order to help avoid the occurrence of a matching Section 16(b) purchase and sale.

**Do the new rules require that Section 16 reports be filed electronically or be posted on the company's web site?**

The Sarbanes-Oxley Act requires that beginning no later than July 30, 2003, Section 16 reports must be filed electronically with the SEC and posted by companies on their web sites. The SEC indicated in its August 27, 2002 release that it intends to require electronic filing of Section 16 reports in advance of this deadline. The SEC has encouraged insiders to file electronically in advance of the actual requirement to do so and, to that end, will accept reports that are not presented in the standard box format and that omit the horizontal and vertical lines separating information items, as long as those items are in the proper order.

If an insider has not already obtained EDGAR ID codes to file Section 16 reports electronically, the insider will need to file a Form ID with the SEC. The Form ID is available on the SEC's website at <http://www.sec.gov/about/forms/formid.pdf>. Completed forms should be sent by facsimile to the SEC at (202) 504-2474 or (703) 914-4240. The SEC has requested that, when applying for EDGAR ID codes, insiders indicate whether they are also required to file reports with the SEC for any other companies and whether a CIK number has previously been assigned to them by the SEC. If an insider already has EDGAR ID codes, the insider does not need to apply for new ones.

The SEC has also encouraged companies to post their insiders' Section 16 filings on their web sites in advance of the actual requirement to do so.

**Do these new rules apply to insiders of foreign private issuers?**

No. Securities registered by foreign private issuers remain exempt from Section 16.

**When are these new rules effective?**

These rules apply to transactions occurring on or after August 29, 2002. Transactions occurring before August 29, 2002 continue to be subject to the earlier rules. Therefore, for example, a reportable transaction occurring on August 28, 2002 should be reflected on a Form 4 that would be due by September 10, 2002.

**What should we do to respond to these new rules?**

As we discussed in our memo entitled "Change Section 16 Procedures Now to Address Two-Day Deadline for Forms 4," (which can be accessed at [http://www.fenwick.com/pub/corp\\_pubs/Section\\_16\\_Procedures.htm](http://www.fenwick.com/pub/corp_pubs/Section_16_Procedures.htm)), companies that assist their insiders in responding to Section 16 requirements need to revise their Section

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16 policies and procedures in order to be able to respond to the new two-day filing deadline. Some of the actions that companies and insiders should consider are:

- evaluating the adequacy of the company's compliance staff;
- ensuring that the company's compliance staff receives available information and resources;
- requiring pre-clearance of all transactions by Section 16 officers and directors;
- requiring that insiders notify the company immediately of any transactions by them or by related parties;
- working with insiders' brokers to obtain transaction information immediately;
- obtaining powers of attorney from insiders to make Section 16 filings; and
- evaluating filing methods for Section 16 reports.

If you have any questions about these rule changes or other current developments, please call any member of your Fenwick & West team or Horace Nash ([hnash@fenwick.com](mailto:hnash@fenwick.com)), Eileen Duffy Robinett ([erobinett@fenwick.com](mailto:erobinett@fenwick.com)), Robert Freedman ([rfreedman@fenwick.com](mailto:rfreedman@fenwick.com)), Scott Spector ([sspector@fenwick.com](mailto:sspector@fenwick.com)), Dan Winnike ([dwinnike@fenwick.com](mailto:dwinnike@fenwick.com)) or Laird Simons ([lsimons@fenwick.com](mailto:lsimons@fenwick.com)), each of whom participated in drafting this update.