

## Two-Day Form 4 Filing Requirement Becomes Effective August 29<sup>th</sup>

The Sarbanes-Oxley Act of 2002 contains a new two-business-day Form 4 filing requirement which becomes effective for transactions occurring on or after August 29, 2002. The new requirement applies as follows:

### Covered Persons

The new filing requirement applies to all Section 16 reporting persons.

### Covered Transactions

In addition to purchases and sales, the new two-business-day requirement applies to any change in ownership, including gifts, stock and option grants, and other transfers. The new requirement also applies to any purchase or sale by a Section 16 reporting person of a security-based swap agreement, as defined under the Gramm-Leach-Bliley Act.<sup>1</sup>

The SEC has indicated that it intends to identify and exempt a narrowly-defined group of transactions for which the two-business-day requirement is not feasible based on objective criteria that would prevent the Section 16 reporting person from controlling (and in many cases knowing) the timing of transaction execution. This group is likely to include:

- transactions pursuant to a single market order that is executed over more than one (but a limited number) of days;
- transactions pursuant to a pre-existing arrangement (such as a Rule 10b5-1 trading plan) under which the timing is outside the knowledge of the Section 16 reporting person prior to the his or her receipt of notice that the transaction has occurred; and
- “discretionary transactions” within an employee benefit plan where the timing or amount is outside the knowledge of the Section 16 reporting person prior to his or her receipt of notice that the transaction has occurred. In addition, the SEC may clarify that it will continue to permit deferred reporting of some exempt transactions.

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<sup>1</sup> A “swap agreement” means any individually negotiated contract, agreement, warrant, note or option that is based, in whole or in part, on the value of, any interest in or any quantitative measure or the occurrence of any event relating to one or more commodities, securities, currencies, interest or other rates, indices, or other assets, but does not include any other identified banking product, as defined in the Gramm-Leach-Bliley Act.

## **Sanctions**

Any late or delinquent Form 4 filings are required to be reported in the proxy statement, as in the past. The SEC has been granted broad authority by the new legislation to seek “any equitable relief that may be appropriate or necessary for the benefit of investors” for violations of any provisions of the securities laws.

## **Compliance**

To ensure compliance, pre-clearance procedures should be adopted and enforced in which Section 16 reporting persons are prohibited from engaging in any transaction involving the company's securities (including a stock plan transaction such as an option exercise, a gift, a loan or pledge or hedge, a contribution to a trust, or any other transfer) without first obtaining pre-clearance of the transaction from the General Counsel or other designated officer. A request for pre-clearance should be submitted to the General Counsel or such other officer at least two days in advance of the proposed transaction. The General Counsel or such other officer will then determine whether the transaction may proceed and, if so, assist in complying with the new reporting requirements. In addition, Section 16 reporting persons should notify the General Counsel or such other officer as soon as a transaction has occurred.

## **Rule 10b5-1 Trading Plans**

Rule 10b5-1 trading plans are permissible so long as the transactions under such plans are reported to the General Counsel or such other officer as soon as the transactions have occurred.

## **Blackout Periods**

Effective January 26, 2003, each Section 16 reporting person will be prohibited from acquiring or disposing, during a “pension fund blackout period,” any company equity security that was acquired by that person in connection with his or her service or employment as a director or executive officer of the company. A “pension fund blackout period” is a period of more than three consecutive business days during which the ability of 50% or more of the participants in a company's 401(k) and other ERISA individual account plans to trade company stock is suspended. In other words, if employees cannot trade in their pension funds, executives and directors cannot trade other securities acquired from the company.

## **Brokers as Gatekeepers**

In order to ensure compliance, companies should consider requiring all Section 16 reporting persons use the same broker and requiring that broker to agree to two requirements:

- not to enter any order (except for orders under pre-approved Rule 10b5-1 trading plans) without first verifying with the General Counsel or such other officer that the transaction was pre-cleared; and
- to report immediately to the General Counsel or such other officer via telephone and in writing (via e-mail or fax) the details of every transaction involving company securities, including gifts, transfers, pledges and all transactions under Rule 10b5-1 trading plans.

## **Periodic Preventive Reminders**

Companies should consider sending periodic preventive reminders, by email or otherwise, to Section 16 reporting persons during the course of the year.

## **Power of Attorney**

In order to enable a company to prepare and file any Form 4 on behalf of a Section 16 reporting person on a timely basis, each Section 16 reporting person should sign a power of attorney authorizing one or more persons, usually the General Counsel and one or two other designated officers, to sign Forms 3, 4 and 5 on his or her behalf.

If you have any questions or comments about this client advisory, please contact **M. Ridgway Barker** at (203) 351-8032 or [mrbarke@kelleydrye.com](mailto:mrbarke@kelleydrye.com), or **Randi-Jean G. Hedin** at (203) 351-8107 or [rhedin@kelleydrye.com](mailto:rhedin@kelleydrye.com).