



Recent SEC Enforcement Actions Over Insider Reporting of Stock Transactions

On September 10, 2014, the Securities and Exchange Commission ("SEC") announced enforcement actions against 13 directors and officers, 10 investment firms and 5 individuals with beneficial ownership in public companies, in connection with delinquent reporting of securities holdings and transactions in company stock. In addition, six publicly-traded companies were also charged for contributing to the filing failures or for failing to report their insiders' filing delinquencies. All but 1 of the 34 persons or entities charged has agreed to settle the charges and pay financial penalties ranging from \$25,000 to \$150,000, with the SEC collecting a total of \$2.6 million.

This enforcement sweep appears to be part of the "broken window" strategy SEC Chair Mary Jo White announced last year, indicating that the SEC intends to "pursue even the smallest infractions." These actions also make it clear that the SEC has the means to follow through. Andrew Ceresney, Director of the SEC's Enforcement Division, indicated that the SEC used "quantitative analytics" to identify repeatedly delinquent filers, likely through the Enforcement Division's Center for Risk and Quantitative Analytics established last year.

Applicable Securities Law Requirements

Section 16(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 16a-3 thereunder require directors, officers and beneficial owners of greater than 10 percent of a company's registered securities (collectively, the "insiders") to file with the SEC initial statements of beneficial holdings on Form 3 within 10 days of becoming an insider, and to file a Form 4 to update that information within 2 business days of a reportable transaction. Exchange Act Sections 13(d) and 13(g) require disclosure of ownership by greater-than-5 percent beneficial owners of a class of a company's equity securities. Additionally, Item 405 of Regulation S-K requires a public company to identify its insiders' delinquent Section 16(a) filings in either its proxy statement or its annual report mandated by Exchange Act Section 13(a) and Rule 13a-1.

Takeaways and Action Items

The SEC's actions represent an unprecedented enforcement sweep in the Section 16 arena, and serve as a reminder to public companies and their insiders of the importance of diligence in the reporting of insider transactions. A review of the orders leads to the following key takeaways:

- *There is little or no defense available for failure to file.* None of the defenses asserted by those charged were accepted by the SEC; including the following:

- **Reliance on others to make the filings.** Many of the insiders claimed that they had relied on others, including the issuer, their broker, or outside counsel, to make the filings. The SEC rejected these assertions, stating that the "insider retains legal responsibility for compliance with the filing requirements, including the obligation to assure that the filing is timely and accurately made."
- **Ignorance of the rules.** One of the officers, a principal accounting officer and controller, claimed that he was delinquent in his filings for seven years because he was not informed by his employer that he was subject to the Section 16 reporting requirements. The SEC rejected this defense, once again asserting the insider's ultimate responsibility for his filings.
- *Issuers that assist insiders with filings can be held responsible for filing delinquencies.* As the SEC noted in several of the orders, "[a]lthough the Commission encourages the practice of many issuers to assist insiders in complying with Section 16(a) filing requirements, issuers who voluntarily accept certain responsibilities and then act negligently in the performance of those tasks may be liable as a cause of Section 16(a) violations by insiders." Five of the six issuers were charged with causing certain of the insider violations through their negligence.
- *An issuer's disclosures under Item 405 of Regulation S-K should be taken seriously.* Five of the six issuers were charged with making misstatements or failing to disclose delinquent filings by their insiders.

In light of these enforcement actions, issuers should consider re-evaluating their internal processes relating to insider transactions, including those related to the identification of insiders and the education of those insiders as to their filing responsibilities. In addition, if an issuer has undertaken to assist its insiders with Section 16(a) filings, the procedures for the collection of transaction information and timely preparation and filing of the required reports should be reviewed. Even if the processes are found to be sufficient, issuers should consider sending reminders to insiders regarding their responsibilities and how transaction information should be communicated. Finally, issuers should annually review their insiders' Section 16(a) filings to ensure accurate disclosure under Item 405 of Regulation S-K.

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Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, please contact your Jones Walker relationship attorney or:

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